T135 TAIT, R.E. Product liability in New Zealand.

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PRODUCT LIABILITY IN NEW ZEALAND

LLB(HONS) RESEARCH PAPER

LAW AND SOCIAL POLICY (LAWS 539)

LAW FACULTY

VICTORIA UNIVERSITY OF WELLINGTON

1996

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ABSTRACT

This paper was inspired by a preliminary report on product liability in New Zealand that the writer prepared for the Ministry of Consumer Affairs in 1995. In overseas jurisdictions there is a substantial body of theory and law on the subject of product liability, which has been recognised as a separate area of the law for over 30 years.

New Zealand has never considered product liability to be a unique area of the law, distinct from traditional tort and contract theory and assorted statutory provisions. Although product liability was briefly considered by the Torts and General Law Reform Committee in 1974, remarkably little analysis has been carried out in respect of New Zealand's product liability legal and policy framework.

The paper aims to remedy this state of affairs by using the overseas experience of product liability to assess the adequacy of New Zealand's approach to product liability, in terms of the international standardisation of laws and internal consistency within New Zealand, and against "ideal" policy goals.

Most of New Zealand's trading partners have reformed their law to such a degree that universal principles and standards have developed. The paper will consider whether New Zealand should become a part of this standardisation process, providing an introduction to the vast area of the law that product liability is becoming in other countries, and advancing options that New Zealand may consider in the future.

The following discussion does not purport to be a comprehensive account of product liability in New Zealand in the past, present and future. Instead it aims to provide the reader with a grasp of the issues involved so as to stimulate further consideration and analysis of specific aspects of product liability.

WORD LENGTH

The text of this paper (excluding contents page, footnotes and bibliography) comprises approximately 15800 words.

I INTRODUCTION - CONSUMER POLICY

A The Development of Consumerism

A primary concern of consumer policy is to redress power imbalances in consumer transactions. There are two parties in the power struggle - consumers and producers. Consumers are those who "consume" the goods and services provided by the producers.

> **consumer** *n.* **2** a user of an article or commodity. A buyer of goods or services.[1]

As individuals we are all consumers, because we are constantly purchasing, acquiring or using goods or services that have been produced by others.

Both elements of the above definition will play a part in the following discussion of product liability in New Zealand. The person who suffers injury or loss will often be the purchaser of the defective goods that caused the loss, or the donee of those goods. However, this paper will illustrate that adopting a restrictive definition of "consumer" in the product liability context can lead to anomalous results when considering available means of redress. In this paper, a consumer will be "a user of an article or commodity" unless stated otherwise. The paper is primarily concerned with non-commercial consumers, or consumers who use goods ordinarily acquired for personal, domestic or household use or consumption.

Traditionally, consumers have been at a disadvantage *vis-à-vis* the producers. Consumers as individuals typically tend to be ill informed about the goods they buy, ill informed about their rights in relation to those goods, lacking in any substantial bargaining power and therefore unable to exercise any real control over the producer. *Caveat emptor*[2] developed at a time when traders and buyers met in the open markets to buy and sell goods. Goods were not technologically complex, and purchasers could readily detect inferior quality goods by a visual inspection. With this in mind the courts were reluctant to go beyond the contract in cases where goods subsequently became manifestly defective.

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1 *The New Shorter Oxford English Dictionary* L Brown (ed) (Clarendon Press, Oxford, 1993).

2 A phrase literally meaning "Let the buyer beware". This was a concept developed by the judiciary to give effect to the notion that ultimately the consumer was responsible for his or her own purchasing decisions.

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To go beyond the contract involved interfering with the rights of parties to make contracts at arms length, which would have affected the "sanctity" of the contract that had been made. The courts therefore sought to preserve arms-length commercial arrangements without undue interference. The onus was placed on buyers to ensure that what they bought was not defective.

During the twentieth century, producers have been developing and manufacturing goods which are increasingly complex. Modern consumers generally have insufficient technical knowledge to determine the quality of the goods they buy simply by a visual inspection. Latent defects may not manifest themselves for some time after purchase. The courts began to recognise the difficulties associated with the dawn of the technological era and gradually developed implied contractual terms at common law to temper the harsh effects of the outdated *caveat emptor* doctrine. Notions such as "merchantability of goods" and "fitness for purpose" were invoked and became more commonplace until New Zealand eventually codified these concepts, amongst others, into the Sale of Goods Act 1908. Until the Courts began to erode the concept of *caveat emptor* the power balance between buyer and seller lay strongly in favour of the seller. This was the genesis of modern consumer policy.

B The Nature of Consumer Policy

1 Protectionism

Consumer policy is inseparably involved with protectionist measures. The key is in deciding to what extent the law should protect consumers from the vagaries of the market. Traditional free market economics considers that a market will function most effectively with minimal regulatory interference from the State. The theory hinges on the notion that the market will be "self-regulating" - consumers will have control over the market and the producers by exercising choice in the form of purchasing decisions. Although it may be a valid theoretical model it is perhaps too optimistic, as it presumes the existence of perfect market conditions. In reality the operation of the market is far from perfect. Market failure is inherent in our system - consumers are not sufficiently active in pursuing their rights and the large power imbalances mean that consumers do not adequately meet their required role in the *laisser-faire*/free market theory.

Consumer policy therefore reflects the pragmatic notion that consumers are not sufficiently powerful to survive in a market unassisted by regulatory measures. For example, consumer policy regulates some businesses by imposing minimum safety standards on certain classes of products.[3] However, it also recognises that consumers will and do make bad purchasing choices even if they have sufficient information available on which they can base a purchasing decision. In this situation the law may also provide a remedy.[4]

Consumer policy aims to regulate the market to the least degree necessary, so as to empower consumers, redress imbalances, and at the same time, create a competitive, functional market in which consumers play an important role.

2 *Competing Policy Goals*

Consumer policy must therefore balance two competing policy goals. First, it recognises that consumers need enforceable rights to protect their individual social and economic interests. This reflects the protectionist role of consumer policy. It provides consumers with a crutch upon which to lean when dealing with producers/manufacturers.[5]

Second, the protectionist function must be weighed against the overall economic interests of the market. Excess regulation can inhibit trade and hinder a fully competitive market.[6] Consumer policy realises that an excessively interventionist approach is not economically sound in the long run as it may ultimately act to the detriment of the consumer.

Consumer law is the product of this balancing act.

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3 See for example Part III of the Fair Trading Act 1986 which allows for the creation of product safety standards.

4 For example, see the Consumer Guarantees Act 1993 generally.

5 In this paper, the "manufacturer" will often include the designer. Certain product liability issues will arise in respect of designers in particular. These will be addressed separately.

6 Observe the application of the Commerce Act 1986 by the Commerce Commission, which regulates trade to the minimum degree necessary in order to foster fair competition. This is particularly relevant in the telecommunications industry at the present time.

C New Zealand's Approach to Consumer Policy

Those who create consumer policy in New Zealand aim to achieve a competitive market involving the least possible Government intervention, while at the same time protecting consumers' fundamental rights and empowering them so as to enhance the functioning of the market.[7]

New Zealand has adopted a piecemeal approach towards the implementation of consumer policy. The legislature, in implementing such policy, has preferred not to create broad, "umbrella" consumer laws. Rather, the approach has been to address particular problems as and when they arise. Consequently, New Zealand has a wide range of different laws relating to consumer policy which address specific issues.

Mulholland has suggested that legislation which serves to alienate the business community in this country will not find favour;

> The Government relies upon the business community for the implementation of much of its policy and it would not serve any Government to unnecessarily irritate the business community.[8]

Although consumer policy can sometimes be difficult to implement in New Zealand, it can be achieved through a combination of several factors. First, by clearly illustrating a need for reform, and second, by consumers voicing their concerns and making themselves heard in a co-ordinated approach to lobbying.[9]

Product liability reform is the focus of this paper. Many manufacturers and members of the business community will view product liability reform as being inherently adverse to their interests. As can be seen from recent debates in Australia on this issue prior to the enactment of reform in that country in 1992, the industry sector was strongly opposed to the proposed reform.[10]

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7 C Stigley "Fair Trading: The New Zealand Experience" Conference Address, JASCA Conference, Kyoto, Japan, 1994.

8 RD Mulholland *Consumer Law in New Zealand* (Dunmore Press, Palmerston North, 1982) 22.

9 An example of such a co-ordinated approach can be seen in the current efforts of the Choice in Accident Compensation Campaign towards the review of accident compensation legislation.

10 For example, "No Justice in Law Reform Proposals: Business Leaders" *Australian Financial Review*, , Australia, 11 September 1989, 15; and "The Perils of Product Liability" *Business Review Weekly*, Australia, 8 December 1989, 94.

It would come as no surprise that any such reform in New Zealand may be met with similar resistance and therefore product liability reform is low on the list of political priorities.

Nevertheless, as will be seen in the remainder of this paper, there is a need for some degree of reform in this area. It will consider some of the issues facing policy makers when considering the current state of product liability in New Zealand. It will also consider options for product liability regulation in the future.

II PRODUCT LIABILITY

A Product Safety v. Product Liability

The promotion of consumer safety is a key objective of consumer policy. Consumer safety policy has two components.

1 Product safety regulation

Product safety measures focus on actively promoting the distribution of safe products onto the consumer markets. These measures aim to prevent or minimise the risk of entry of unsafe products. Product safety is generally proactive, aimed at *prevention* of injury by imposing uniform regulatory standards on manufacturers. These measures generally create offences and carry punitive provisions for non-compliance.[11]

2 Product Liability

In any consumer protection framework, product liability is a strongly protectionist measure. The principle of product liability recognises that no *preventative* framework can provide absolute protection for the consumer. Rather than having a direct punitive focus against the offending manufacturer, product liability provides rights and remedies to compensate victims when an unsafe product causes injury or damage after finding its way into the hands of the consumer. Product liability is largely a *reactive* concept, addressing the issue of compensating the individual when damage or injury does occur. However, an important consequence of imposing product liability is the potential deterrent effect which ensures that manufacturers take care in the production of goods. Product safety and product liability measures complement each other in this way.

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[11] See for example Part III of the Fair Trading Act 1986 and its relationship with s40 "Offences".

Whether or not the consumer takes all possible care, the reality is that some products will inevitably fail to meet up to the expected standard. When products fail, they are capable of causing injury, death or damage to other property and economic loss.

B The Policy Underlying Product Liability

In practice, no amount of regulation will be able to prevent some defective products from finding their way onto the market. Where these products cause injury or damage, and the loss was attributable to the actions of the manufacturer rather than the consumer, then the manufacturer is generally required to make good that loss.

Consumer policy imposes this obligation on the manufacturer on the basis of social and economic policy. If individuals were required to bear the full cost of injury or damage themselves, the potential for drain on welfare systems is increased due to the individual's possible inability to work for a long period of time, requirements for healthcare, and inequitable financial losses which the individual is left to bear. Under this scenario, the loss is not allocated to the person best able to avoid it, and it would create unacceptable direct losses for the individual, and indirect losses for the State and the market as a whole.

Policy makers believe that liability for such loss should lie with the person or persons who are in the best position to avoid the possibility of loss.[12] This premise has several practical policy benefits.

First, the loss is generally borne by persons (the manufacturer) who are more capable of bearing the loss than the individual consumer. Through pricing mechanisms and insurance, the cost is indirectly borne by the consuming public as a whole.[13] Goldring notes that this cost/price mechanism "requires the manufacturer or supplier to make a decision which reflects 'optimal'

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12 Law Reform Commission of Australia *Product Liability - Discussion paper No. 34* (Law Reform Commission, Sydney, 1988).

13 Note that community responsibility was a fundamental tenet of the accident compensation scheme as originally enacted in 1972. See the findings of the Royal Commission to Inquire into and Report upon Worker's Compensation *Compensation for Personal Injury in New Zealand: Report of the Royal Commission of Inquiry* (Government Print, Wellington, 1967).

levels of loss prevention".[14] The result is effective pricing which reflects the true cost of the product. Accordingly, those who receive the benefits from the production or use of the product collectively bear the costs associated with that product. Ultimately the product's survival on the market depends on competitive pricing.

Second, the potential for liability creates an incentive towards the production of goods that will not cause loss. Attributing liability to a manufacturer acts as an indirect regulatory measure. No manufacturer wants to be sued because it may result in a direct financial loss and unwanted negative publicity which will ultimately have an adverse impact on the manufacturer's business as a whole.

The Australian Law Reform Commission concluded that product liability policy has two key objectives:[15]

- The provision of incentives for the optimal level of risk prevention, and
- The efficient provision of adequate and appropriate compensation where goods cause loss because they act in ways that could not reasonably be expected.

These objectives will be adopted as the benchmark policy objectives for the reform issues in this paper.

C Sources of Product Liability Remedies

There are three basic sources of product liability remedies - contract, tort and statutory duty.

1 Contract

Contractual remedies are based on the existence of a contractual relationship between the parties. The policy basis behind contractual remedies is that the parties are entitled to have their

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14 J Goldring "Reforming Australian Product Liability Laws: processes and problems of law reform" (1989) 1 Bond Law Review 193-217.

15 Above n 14, 206.

expectations on the contract fulfilled. Common law and the Sale of Goods Act 1908 give the consumer the right to invoke implied contractual terms of "merchantability" and "fitness for purpose" which can be relied upon in the event that the goods do not match the expected standard or quality.

2 Tort

In comparison, tort law seeks to compensate a person who suffers injury or loss due to a tortious act or omission by another person. As a product liability vehicle, tort law often involves concepts of negligence, or fault-based liability.

Tort theory has a fundamentally different basis to contract theory. Tort law focuses on safety and the rights of individuals not to be harmed by unsafe goods. Contract law acknowledges that contracting parties have a right to expect certain quality standards from the goods they purchase.

Contractual liability protects the economic interests of contracting parties by compensating them for unsatisfied expectations relating to the product. Liability may give rise to consequential damages. Tort liability is not based on the product in question but on the behaviour of the manufacturer, and whether the manufacturer's conduct matches "reasonable" standards of conduct in society, such that the conduct will either be allowed, or not tolerated. Liability is established by way of a cost/benefit analysis, weighing foreseeability of damage and compliance costs against the right not to be injured by another's action.

3 Statutory duties

Statutory duties are imposed on manufacturers by the legislature. They often set out a number of conditions. If one of these conditions is breached, the purchaser will have a right of action under the legislation for compensation. Actions under the Consumer Guarantees Act 1993 fit into this category.

4 *The development of strict liability*

Strict product liability has developed as a hybrid category in recent times. In the United States it was developed through the extension of tort law. In many other countries, in particular, the EU, Australia and Japan, it has taken on characteristics of tort law and statutory obligations. Under a strict product liability system, the claimant does not have to prove that the manufacturer of a defective product was at fault or negligent in some way. Subject to certain defences, the claimant is entitled to compensation from the manufacturer if the claimant can show that the offending product was "defective" according to certain criteria, and that the defect caused loss or injury. Note that strict liability is not the same as absolute liability. Manufacturers will not be automatically liable for all product-related damage or loss. A claimant is still required to identify a defect in the product. Contrast this with negligence, where the claimant must also show that the damage was caused by a negligent act or omission on the part of the manufacturer or some other person.

The policy underlying strict product liability is primarily concerned with compensating individuals for injury and loss. This is a concern it shares with tort law. However, the product liability laws in the countries referred to are enacted into domestic law and have much in common with the "statutory duty" category. These laws are also concerned with the spreading of risk, influencing the making of decisions by business and consumers about what goods are to be produced, what characteristics they should have, what goods should be consumed and how they should be used by consumers.[16] It could be argued that this model has imported some of the "expectation" elements of contract law. The doctrine is concerned more with the behaviour of the defective product that with the behaviour of the manufacturer.

5 *Conclusions*

Product liability remedies have evolved from different theoretical sources which were originally developed to address situations that did not necessarily involve product liability. Each remedy therefore requires the claimant to satisfy a different evidentiary burden and results in a different

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16 Several of these ideas have been drawn from J Goldring, LW Maher and J McKeough *Consumer Protection Law* (Federation Press, Sydney, 1993) 94.

measure of damages, due to the conceptual differences between them. These differences can lead to inconsistencies both in remedy and procedure when applied to product liability situations. Most countries have implemented several of the models into their domestic law at various times. Currently the statutory strict liability model has been finding favour internationally. The various merits and disadvantages of each model will be discussed in more depth later.

This paper will not discuss product safety regulation, which although part of the overall consumer safety framework, is concerned more with preventative and punitive action rather than the rights of injured consumers to seek compensation. Similarly, product liability as stated in the EC Directive is only concerned with consequential loss *resulting* from defective products.[17] This paper will *not* examine remedies available to the consumer for replacement of the defective product itself.[18] The focus of the paper is on the harm caused by the defective product.

D Defectiveness

This paper will frequently refer to "defective products". It is useful to consider what is meant by a defect in this context. Several commentators have categorised defects into these three types.[19]

1 Manufacturing Defects

A manufacturing defect occurs where the product or a batch inadvertently fails due to some miscarriage in the production, transportation or storage process. Products containing such defects may fail to meet up to the manufacturer's usual standards for a number of reasons, including; incorporation of faulty components,[20] misassembly of the product by an employee, an accident in storage or mispackaging.

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17 Article 9 of the Directive of the Council of European Communities on Product Liability 85/374 (25 July 1985).

18 Other actions can be brought for the replacement of the defective product itself. Most of these actions will be based on contract or the Consumer Guarantees Act 1993, as generally only the purchaser of the goods will want compensation.

19 EE Beerworth *Contemporary Issues in Product Liability Law* (Federation Press, Sydney, 1991) 11.

20 For example, a rotor-bolt that was not manufactured to specification and caused a helicopter to crash in *Helicopter Sales (Australia) Pty Ltd* v *Rotor-Work Pty Ltd* (1974) 132 CLR 1.

2 *Design Defects*

A design defect occurs where the design of the product is at fault. It is distinguished from the manufacturing defect on the basis that the defect will be inherent in all examples of the product, and the product does in fact meet the manufacturer's specifications.

3 *Information Defects*

An informational defect will occur where the product will become faulty if used in a certain way, or if certain precautions are not taken, and a warning is not given by the manufacturer. The manufacturer may have an obligation to bring this information to the attention of the consumer.

III PRODUCT LIABILITY IN NEW ZEALAND

A Introduction

As with other consumer issues, product liability has been the subject of a piecemeal approach by the legislature. Unlike many other countries, New Zealand does not have one "product liability" law,[21] but addresses product liability in statutes that are not specifically directed at the issue, and also through the use of traditional common law remedies. This approach will be criticised on the basis that it leads to inconsistencies between rights and remedies in respect of the same defective product.

Damage caused by defective products fits into one of three classes, personal injury, consequential property damage and pure economic loss.

The first category, personal injury, tends to receive the most publicity. As can be seen from the experience in the United States over the past 30 years, personal injury caused by defective products triggers an emotional response in most people due to the high value which our society places on human life. The emotional sympathy for those who are physically injured leads some United States juries to award punitive and compensatory damages at a quantum which New Zealand juries would find hard to comprehend.[22]

The second category, property damage, tends to attract much less attention, but nevertheless creates important rights of action that are upheld by the courts. The third category, pure economic loss, is a developing area of the law characterised by economic loss suffered (for example, loss of future profits) which is not a consequence of any physical harm.[23]

In comparison with other developed nations in the worldwide trading community, New Zealand currently has a unique approach to resolving product liability claims involving personal injury. Due

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21 Most of the EU countries have enacted product liability laws based on the same model, which will be discussed later. Japan and Australia have also recently enacted similar laws.

22 Charlotte Mahlum suffered serious health problems as a result of faulty silicone breast implants. On 29 October 1995 a Texas jury ordered Dow Chemical to pay her $14.1 million in damages, consisting of $3.9 million compensatory damages and $10 million punitive damages.

23 *Junior Books v Veitchi Co Ltd* [1982] 2 All ER 201.

to the existence of a no-fault compensation scheme in respect of personal injury in New Zealand, a practical distinction is drawn between:

- Liability where defective products cause personal injury or death.
- Liability where defective products cause damage or loss to property (consequential property damage) and pure economic loss.

B Remedies where Defective Products Cause Personal Injury: the Accident Compensation Scheme

Consumers who use defective products risk suffering personal injury or even death. New Zealand currently has a no-fault statutory compensation scheme for persons who suffer personal injury that is covered by the Accident Rehabilitation and Compensation Insurance Act 1992 ("ARCIA"). This scheme has effectively shifted the onus of compensating the injured person from the negligent individual to the State via levies on employers, motorists and the taxpayer. This paper will not provide a comprehensive analysis of the scheme, but will concentrate on elements that are relevant to product liability in New Zealand.

New Zealand's first comprehensive no-fault compensation regime for personal injury was enacted in 1972. No other scheme in the world to date has been as broad in its cover and entitlements. After a revamp in 1982, serious reform was carried through in 1992 by the ARCIA. This paper discusses the effect of the ARCIA, being the scheme in force at the time of writing.[24]

1 What Constitutes "Cover" Under the Act?

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24 The ARCIA has come under considerable critical scrutiny since its enactment. Criticisms have been advanced by a variety of different political and non-political bodies, including the Insurance Council of New Zealand, The NZ Business Roundtable and the NZ Manufacturers Federation, all of whom are advocating such reform. See for example "Insurers seek ACC role" *The Independent*, New Zealand, 4 May 1996, 22.

The Act awards compensation to injured persons, regardless of who caused the injury, if certain criteria specified by the ARCIA are met. The Accident Compensation Corporation ("ACC")[25] will provide compensation where a person suffers a "personal injury"[26] in a certain range of circumstances, including:

Section 8(2)(a) accident,

(b) gradual process, disease or infection arising out of and in the course of employment,

(c) medical misadventure,

(d) consequence of treatment for personal injury.

In product liability cases, the most likely way the Act's cover will extend to personal injury is by accident and medical misadventure. The Act defines "personal injury", "accident"[27] and "medical misadventure".[28]

A personal injury is essentially a physical injury to a person and any mental injury suffered by that person that is an outcome of those physical injuries.

"Accident" is defined in a way that is open to several possible interpretations.[29] The most common interpretation involves the application of a force or resistance external to the human body and is a specific identifiable event or series of events.

An injury will happen as a result of "medical misadventure" if the injury was due to "medical error" or "medical mishap" at the hands of a "registered health professional".[30]

2 *Removal of the Right to Sue*

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25 The ACC is the body set up to administer the handling of personal injury claims under the ARCIA.

26 "Personal injury" is defined in section 4 of the ARCIA.

27 "Accident" is defined in section 3.

28 "Medical misadventure" is defined in section 5.

29 See section 3 of the ARCIA.

30 These terms are all defined in the ARCIA; "medical error" and "medical mishap" - section 5(1), "registered health professional" - section 3.

In common with both the 1972 and 1982 Acts, the ARCIA removes the right to sue for compensatory damages in respect of personal injuries that are covered by the Act.[31] A person who suffers personal injury falling within the Act's cover is limited to suing for exemplary damages if this is appropriate.

The natural consequence of this restriction is that a person whose injuries fall outside the cover of the ARCIA may seek compensatory damages in the courts. Due to the narrower definitions of "personal injury" and "cover" in the 1992 Act, a number of injuries that would have been covered by the previous two Acts are now excluded from the cover of the 1992 Act. If the Act does not cover the injury then the injured person will be entitled to bring a claim for common law compensatory damages in a New Zealand court.[32]

Under section 14(5) of the ARCIA, the court now makes the ultimate determination about whether the injuries suffered are covered by the Act. Prior to 1992, this issue had to be referred to the ACC for determination. Under the 1992 Act the ACC must be a party to any proceedings that determines this question.

3 Exemplary Damages

Recent developments in New Zealand's common law mean that in future a plaintiff may be able to bring a successful action for exemplary damages in a negligence case. None of the accident compensation Acts have barred a common law claim for exemplary damages where the injury was covered by the Act.[33] Courts have traditionally awarded exemplary damages where there is aggravating behaviour that warrants a measure of damages which can be awarded against a defendant as a form of punishment for "high-handed" behaviour. Claims for exemplary damages have not generally been available in actions based on claims of negligence, on the grounds that the application of force was not intentional.[34] However, the recent case of *Akavi v Taylor*[35] has

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31 This prohibition is stated in section 14 of the ARCIA.

32 Subject to the injured person's ability to state a tenable cause of action such as negligence.

33 *Donselaar v Donselaar* [1982] 1 NZLR 97.

34 See *Taylor v Beere* [1982] 1 NZLR 81, per Somers J.

suggested that "reduced availability and quantum of accident compensation may lead the courts to extend the concept of negligence and permit common law damages to be awarded."[36] In the most recent statement on exemplary damages in New Zealand at the time of writing, Tipping J has noted that "it is not a proper function of the Courts to develop the law of7 exemplary damages so as to remedy any perceived shortcomings in the statutory scheme".[37]

Australian courts have extended the award of exemplary damages to include negligence cases in certain circumstances. In *Coloca v BP Australia Ltd*,[38] the Court held that the recovery of exemplary damages was governed by the conduct of the wrongdoer and not the nature of the tort.

Several New Zealand cases have considered the possibility of awarding exemplary damages in negligence situations.[39] To date the only New Zealand case in which exemplary damages have actually been awarded to a plaintiff in this situation is *Somerville v McLaren Transport.*[40] In this case the defendant (automotive garage) knowingly ignored safety procedures that should have been used to prevent an over-inflated tyre exploding and causing injury to bystanders. The decision of Everitt DCJ to award the plaintiff $15,000 exemplary damages was upheld on appeal by Tipping J, who, after a detailed and practical analysis of Commonwealth law relating to exemplary damages, clarified the current exemplary damages test into the following statement,

> Exemplary damages for negligence causing personal injury may be awarded if, but only if, the level of negligence is so high that it amounts to an outrageous and flagrant disregard for the plaintiff's safety, meriting condemnation and punishment.[41]

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35 [1995] NZAR 33. See also Blanchard J's comments in *Boustridge v Attorney-General* Unreported, 29 September 1993, High Court, Auckland Registry, CP 54/93.

36 See *Akavi,* above n 35, 33.

37 See below n 40, 20.

38 (1992) ATR 81-153.

39 See for example *Akavi v Taylor* Preston, above n 35, *Boustridge v Attorney-General* above n 35, *Iverson v Zendel Industries* Unreported, 8 June 1993, High Court, Auckland Registry, CP 2171/91, *W v Counties Manukau Health* Ltd [1995] 2 NZLR 560. These cases all involved strikeout applications.

40 Unreported, 13 August 1996, High Court, Dunedin Registry, AP 2/96.

41 Above n 40, 23.

This decision appears to have laid the groundwork for plaintiffs suing for exemplary damages in personal injury claims arising out of negligence. The development is significant for product liability claims in New Zealand. If a manufacturer knows that a negligent manufacturing process is in place but refuses to remedy the problem because compliance costs are high, then courts might be inclined to award exemplary damages if a product subsequently causes injury.

Example

Manufacturer produces 200,000 widgets and sells them to consumers. Manufacturer hears of several claims from consumers who say that they have been injured when a component part of the widget has broken. Manufacturer has knowingly incorporated a design defect into the widget to cut down costs in the form of a low quality component which may cause breakages through normal use in up to 80% of the total widgets sold (totalling around 120,000 widgets). Manufacturer also fails to warn consumers of the defect and decides that it will not recall the widgets because of the cost and time involved in doing so. Manufacturer believes that although there is a reasonably high risk that a number of people will be injured by the widget, ACC will pick up the cost of those claims and Manufacturer will not be directly liable.

In this situation, Manufacturer was arguably negligent in knowingly incorporating an avoidable defect, in failing to warn the consumer and in failing to order a recall of the widgets. Because the faulty widgets cause physical injury, the injured persons are covered under the ARCIA. However, due to the fact that the injury is not too serious, these people receive hardly any compensation under the ARCIA. It is conceivable that the injured persons may be able to bring a successful claim for exemplary damages against Manufacturer on the grounds that Manufacturer deliberately ignored the problems that were being caused by defective widgets.

4 *Product Liability falling outside the scope of the ARCIA*[42]

If it is arguable that a plaintiff's injuries are not covered by the ARCIA, then the injured person can bring a proceedings in a New Zealand court without reference to the ARCIA in the statement of claim. In such situations the plaintiff is not required to prove that the ARCIA *does not* apply.[43]

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42 Most of the examples given in this part of the paper are necessarily speculative as cases on point have not arisen in the short time since the enactment of the 1992 regime. Examples cited are possible situations which might fall outside the scope of the Act. The definitive answers will turn on judicial interpretation of the relevant sections of the Act. For a discussion of situations which may fall outside the cover of the Act see also S Todd and J Black "Accident Compensation and the Barring of Actions for Damages" [1993] 1 Tort Law Review 197, and R Harrison *Matters of Life and Death: the Accident Rehabilitation and Compensation Insurance Act 1992 and Common Law Claims for Personal Injury* (Legal Research Foundation No.35, Auckland, 1993).

43 D Rennie *Brooker's Accident Compensation in New Zealand* (Brookers, Wellington, 1992), 2A-4.

Instead the defendant must prove that the injury *does* fall within the cover of the ARCIA. The court must then determine the issue after hearing evidence from the ACC.

Examples of product liability situations that might not covered

***No personal injury under the Act* -**

Heart attacks and strokes

Certain injuries such as heart attacks and strokes are generally not covered by the ARCIA.[44] It is conceivable that defective goods may cause this type of injury in certain circumstances, meaning that the injured person could try to recover damages if the facts give rise to a cause of action. For example, a washing machine with a defective bearing could strike a wall that may cause a shock-induced heart attack in a susceptible person.

Nervous shock

If an occurrence results in nervous shock that is not a consequence of a physical injury, then the injured person could bring a common law damages claim if a cause of action is available. A victim of mental trauma could bring a compensation claim where the trauma was the direct result of witnessing negligently caused injury to another person, for example if a negligently manufactured winch caused building materials to be dropped onto a person standing nearby.[45] Direct shock could be caused by a product exploding, with resulting nervous shock but no physical injury.

***Expressly excluded from cover under section 10* -**

Use of teeth

Personal injury to teeth that is caused by the natural use of those teeth is not covered by the ARCIA.[46] Teeth might be damaged by a product during the natural use of those teeth. For example, biting into a pie with a bolt in it could cause damage to teeth that would not be covered by the ARCIA.[47] Under current New Zealand law, the bolt-biter could be compensated under the Consumer Guarantees Act, Sale of Goods Act or a common law negligence action if appropriate.

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44 Under section 4 of the Act, heart attacks and strokes are only covered by the Act if they are the result of medical misadventure or are work related.

45 Depending on the interpretation of section 14(1) this claim may or may not be barred as arising directly or indirectly out of personal injury to another person.

46 Section 10(2)(b).

47 This occurred in *Partner v ARCIC* Unreported, 20 February 1995, High Court, Auckland Registry, 180/93. (Blanchard J)

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Gradual Process or disease that is not in the course of employment

Section 10 expressly excludes from cover any personal injury that is caused by gradual process, disease or infection that is not employment related. A person might have a common law cause of action where long term exposure to a negligently manufactured computer screen resulted in a blood disease due to excessive radiation levels. Or, the use of a badly designed exercise machine over a period of time, which causes personal injury. In this case the victim might not be able to point to a specific event or series of events that caused the injury. On the basis of developments in the United States it may even be arguable that a cigarette manufacturer could be sued in some circumstances.

A cause of injury which is not an accident, and cover is not provided elsewhere in the Act

Under section 3(e) a personal injury will be caused by accident if it involves the absorption of any chemical through the skin within a defined period of time not exceeding one month. Imagine a situation where a manufacturer produces a hand cleaner which causes injury by absorption through skin over a period exceeding one month. In this case there is unlikely to be any cover under the ARCIA.[48]

5 *Medical Product Liability*

The practice of medicine is a field in which product liability claims may arise due to the nature of the drug and medical product manufacturing industries.

An injured person may have a common law claim against a manufacturer where a medical product is found to be faulty due to negligence during the manufacturing/research process. If there are no circumstances to put the health professional on notice then the use of the product is unlikely to constitute "medical error" for the purposes of the Act.[49] If a product has received the requisite government approvals then a health professional might reasonably infer that the product is safe.

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48 Above n 43, 2A-21.

49 "Medical error" is defined in section 5(1) as "the failure of a registered health professional to observe a standard of care and skill reasonably to be expected in the circumstances."

The defect may give rise to a civil action unless the result of the defect can be classified as a "medical mishap".[50]

A current example is the use of HGH (Human Growth Hormone) as a form of treatment. The use of this treatment has recently been linked to occurrences of Creutzfeld-Jakob Disease.[51] A disease such as this caused by gradual process would be *prima facie* excluded from cover under section 10. If the disease falls within the range of medical mishap then there is cover, otherwise a CJD sufferer might try to bring an action against the manufacturer of the drug.

Similarly a claim may arise against a healthcare provider or manufacturer where a blood product causes the recipient of the blood to contract Hepatitis or HIV where:

a) The blood was not given as part of treatment for personal injury[52], and

b) The situation did not fall into the category of medical misadventure.

B Remedies for Consequential Property Damage and Pure Economic Loss

1 Consumer Guarantees Act 1993

The Consumer Guarantees Act 1993 ("CGA") came into force in New Zealand on 1 April 1994. It falls within the "statutory duties" model of product liability under which liability is strict.

The CGA protects consumers by providing statutory guarantees and remedies in respect of goods and services supplied to consumers in trade. The CGA can also provide relief to consumers where defective goods cause damage to property other than the defective goods themselves.

"In trade"

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50 "Medical mishap" is defined in section 5(1).

51 "Lawyer hopes to contact CJD sufferers here" *The Evening Post*, Wellington, New Zealand, 26 April 1996, p 19.

52 In which case cover would be provided under section 8(2)(d).

The Act applies to transactions where a supplier supplies goods to a consumer. A supplier is a person who supplies goods to a consumer "in trade". This means that the supplier must be in the business of supplying goods of that kind.[53]

"Consumer"

A consumer is a person who "acquires from a supplier goods or services of a kind ordinarily acquired for personal, domestic, or household use or consumption."[54] There are several exclusions. A consumer is not a person:

- who acquires goods for the purpose of resupplying them in trade;
- who will consume the goods in the course of a manufacturing process; or
- who will use the goods to repair other goods or fixtures in trade.

This definition tends to exclude most commercial consumers who are left to fend for themselves using contract or tort actions. A consumer "acquires" goods by purchasing, exchanging or being given the goods. Leases and hire purchase arrangements are also included.[55]

Consequential Loss Provisions

The primary focus of the CGA is to provide post-sale warranties in respect of the goods themselves. Section 6 provides a guarantee that the goods will be of acceptable quality. This guarantee supersedes the implied warranty of merchantable quality referred to in section 16 of the Sale of Goods Act 1908 ("SGA"). If goods fail to comply with this guarantee (section 7), the consumer has a number of remedies in respect of the goods themselves. A key characteristic of acceptable quality is that the goods must be safe.

In addition to remedies in respect of the goods themselves, remedies are also available where the defective goods cause loss to other property. Damages can be obtained from either the supplier or the manufacturer/importer of the goods. The designer and other parties who play a part in the

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53 Section 2 of the CGA defines "supplier".

54 Section 2 of the CGA defines "consumer".

55 See definition of "acquire" in section 2.

manufacturing process cannot be targeted under the CGA. The policy basis for this is to enable the consumer to target the parties who actually make and supply the product.

The CGA will apply to manufacturing defect, design defects and informational defects if the existence of the defect means that the product falls short of being of acceptable quality.

> The consumer may obtain from the [supplier/manufacturer] damages for any loss or damage to the consumer resulting from the failure [of the goods to comply with the guarantee] (other than loss or damage through reduction in value of the goods) which was *reasonably foreseeable* as liable to result from the failure.[56]

Provided the CGA applies, this section should cover a personal injury if the ARCIA does not. Where the ARCIA applies, section 14 of the ARCIA prevents an action being taken by the injured person to recover compensatory damages.

Pure Economic Loss

The consequential loss provisions will compensate the consumer whose property is damaged by the behaviour of a defective product. The provisions also may extend to consequential loss of profits. It might be argued that loss of opportunity is covered by the provisions to some extent, to take account of loss of income and opportunities for greater future income. In reality, the manufacturer's liability to account for pure economic loss may not be as great as it seems because many potential business claimants will not be consumers under the Act

Scope of Cover under the CGA

Only the consumer (as defined in section 2 of the CGA) can claim damages under these provisions. This means that a person who did not "acquire" the goods cannot claim for consequential loss if

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[56] Section 18(4) gives the consumer a remedy against the supplier for consequential loss. Section 27(1)(b) provides a similar remedy against the manufacturer.

goods belonging to another person cause damage.[57] "Innocent bystanders" cannot claim under the CGA for damage caused to their property by a product that belongs to someone else.

The CGA has been in force for a relatively short time. To date there is no case law on the application of the product liability provisions in sections 18 and 27 of the Act. The following example arose by application of the Sale of Goods Act 1893 (UK).[58] The CGA would now govern this type of situation. This case is an example where a plaintiff was awarded damages for consequential loss in the type of situation anticipated by the CGA. Under the CGA the action could be brought under section 18 or section 27 (the defendant was both supplier and manufacturer of the defective goods).

Example: ***Wilson and anor.*** **v** ***Rickett Cockerell & Co Ltd*** **[1954] 1 QB 598.**

"Coalite", a manufactured fuel, was supplied by the defendant coal merchants to the plaintiffs. The coal was to be burned in the fireplace to heat the plaintiff's house. The fire was made up using the coal and was lit. An explosion in the grate occurred due to the presence of an explosive substance in the consignment of Coalite. This explosion caused damage to the plaintiff's dining room and furniture in that room.
The plaintiffs claimed against the supplier for the damage to the room and furniture. The Court held that although only one piece of coal was defective, the whole consignment did not satisfy the implied condition of merchantable quality imposed by section 14(2). The plaintiffs were awarded damages for their losses.

2 *Contract law / Sale of Goods Act 1908*

The Privity Problem

Where the product that caused the damage is subject to a contract between the injured person and the seller, the consumer may be able to bring a civil action seeking damages against the seller for breach of contract. There must be a contractual nexus between the claimant and another party, who is usually the supplier, and the defective product must be the subject of the nexus.

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57 Subsequent purchasers of the goods and donees are considered to have acquired the goods for the purposes of the Act.

58 Although this example is taken from the experience in the United Kingdom, it is equally applicable in New Zealand as the Sale of Goods Act 1908 (NZ) was modelled on the British version.

The doctrine of privity of contract severely limits the effectiveness of this remedy because this doctrine only those who contract to buy the goods can sue. They can only sue the person from whom they bought the goods. The reality in most cases is that the consumer is limited to seeking compensation from the retailer, because the manufacturer is probably not a party to the contract.

Although New Zealand has the Contracts (Privity) Act 1982, which allows parties outside the contract to sue as if they were a party to the contract, its application is limited by the requirement that the third party be a "beneficiary" of the contract between the actual parties. It could not be said that a consumer is a beneficiary of a contract of supply between a manufacturer and a retailer.

Sale of Goods Act 1908

The SGA implies a condition of merchantable quality into contracts for the sale of goods.[59] If the goods do not meet with this standard then the condition has been breached. The purchaser can bring an action for breach of contract against the seller.[60]

Section 48 of the CGA amends the SGA, so that where the guarantees in the CGA apply, this Act has primacy over the SGA. Consequently, nothing in section 16 of the SGA (merchantable quality) will apply to the goods if the CGA applies. However, the SGA will continue apply to transactions where the buyer of the goods is not a consumer (as defined in the CGA), or where the CGA does not apply for some other reason. An example of this would be where the buyer purchased the defective goods for the purpose of resupplying them, or using them in a manufacturing process.

Under contract law the buyer can recover both the cost of the defective goods and damages for consequential loss. The loss must not be too remote. The damage for which compensation is sought must have been within the reasonable contemplation of the contracting parties as a serious

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59 This condition is implied into contracts relating to sale of goods by section 16(b) of the Act.

60 Section 54 gives the buyer various rights of action against the seller for a breach of warranty. The SGA restates the common law position that the buyer can sue the seller for damages.

possibility that might result from the breach, at the time the contract was made.[61] The loss must have been directly caused by the breach (in this case, a defect).

Example
X is an electrical appliance retailer. X regularly buys televisions from Y, a manufacturer of televisions, for the purposes of selling them at retail price. X often switches the televisions on for display purposes. One day a television explodes for no apparent reason. The explosion causes damage to other goods on display in the store. X was using all the televisions in an ordinary, reasonable way. X wishes to recover the cost of the damage to the other appliances in the store. The defect can be traced back to the components of the television itself. Can X recover from Y?
X would be able to sue Y in contract for breach of the implied condition of merchantable quality. X would probably be able to gain compensation for the damage to the other appliances. It would be within the reasonable contemplation of Y that if a defect in a television caused the television to explode in X's store, other goods would most likely be damaged.

3 *Tort Remedies: Negligence*

In practice the tort action may be more useful than the contract action because the lack of privity does not bar a claim against the manufacturer of a defective product. The idea of negligence as a means of obtaining a remedy in product liability cases was introduced by *Donoghue v Stephenson,*[62] in which the injured plaintiff sued the manufacturer of a bottled drink that contained the remains of a snail. Consuming the drink had caused the plaintiff to become ill.

Requirements for an Action

To bring a successful claim the plaintiff must first establish that the manufacturer/designer/distributor was negligent, by attributing fault to that person. This task is not

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61 The principles governing remoteness of damage for breach of contract were fully considered in the case of *Hadley v Baxendale* (1854) 9 Exch 341.

62 [1932] AC 562.

easy because the plaintiff in most product liability cases will have no direct access to the manufacturing or design process. The plaintiff must prove four requirements: [63]

(i) That the defendant owed the plaintiff a duty of care. Was the kind of damage in question reasonably foreseeable as a real risk?

(ii) That the defendant breached this duty of care. Would a reasonable person in the position of the defendant have taken further steps to avoid the risk of harm?

(iii) There must be physical harm (or pure economic loss in some circumstances).

(iv) The breach of the duty of care must have caused the harm.

In the case of manufacturing defects, a plaintiff would have to show that a person in the production chain was negligent. This could be a primary producer, a component manufacturer, the manufacturer of the end product, a designer, a distributor or anyone else involved in the process by which the product is made, stored or delivered into the hands of the consumer. Compare this to the CGA which only allows the plaintiff to sue the supplier or the manufacturer/importer.

Design defects may pose a more difficult problem for consumers. The courts will apply a form of cost/benefit analysis to determine whether the reasonable manufacturer would have incorporated the defect into the design.

To impose absolute liability on manufacturers for design defects would hinder technological progress. Assessing whether the manufacturer followed a standard of "reasonableness" means that consumers must tolerate a degree of defectiveness, so long as the defect is not unreasonable as compared to the practices of other manufacturers. This approach has the benefit of providing manufacturers with a benchmark against which to assess their products, and allows for some progress.

For the consumer, it is not so attractive because it acknowledges that some accident will go uncompensated because the defect appeared "in accordance with reasonable industry practice."

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63 A complete discussion of the law relating to negligence is beyond the scope of this report. For a comprehensive discussion of negligence in New Zealand see SMD Todd (ed) *The Law of Torts in New Zealand* (Law Book Company, Sydney, 1991).

A duty exists at common law requiring manufacturers to either warn consumers of defects of which they become aware, or withdraw the product from the market altogether.[64]

Res Ipsa Loquitur

Some countries have made the plaintiff's burden easier by reversing the onus of proving negligence in product liability cases. This is achieved in common law countries by the doctrine of *res ipsa loquitur*, or "the event speaks for itself". Claimants may attempt to rely on this doctrine in situations where there is virtually no evidence about what happened other than the fact of the event itself.

The doctrine allows the Court to infer negligence by the defendant from the mere happening of an event. Its application can prevent injustice in situations where the plaintiff is unable to precisely identify the defendant's wrongful action. It will only apply when the cause of an accident is unknown at the trial or there is conflicting evidence. This can be useful in situations where the plaintiff has limited access to information about a manufacturing process.

There is debate about the scope of the doctrine's application in New Zealand. It is clear that it must be appropriate to infer negligence from the surrounding circumstances. The accident must be of a kind that does not ordinarily happen if due care is taken.[65] The facts must also suggest negligence by the defendant in particular rather than negligence by some unidentified party. The evidence must support a rational inference that the fault lay somewhere within the control of the defendant or its employees or agents.

In New Zealand the doctrine is not settled. One judicial view suggests that the doctrine places the onus of disproving negligence on the defendant. The other view suggests that the doctrine is a rule of evidence rather than a rule of law.[66] According to the latter view, the rule simply allows negligence to be inferred in appropriate situations. The defendant may be able to reverse this inference simply by suggesting an alternative explanation for the accident or proving reasonable care.

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64 *Wright v Dunlop Rubber Co Ltd* (1972) KIR 255.

65 Above n 63, 282.

66 Above n 63, 285.

The negligence action has been used in product liability situations since *Donoghue v Stephenson.* Regardless of whether *res ipsa loquitur* is applied, negligence has a different emphasis to strict liability. To successfully prove negligence the manufacturer must still have been at fault in producing the defective product.

Example

In the Sale of Goods example above, X bought a batch of televisions from Y. A defect in one television caused the unit to catch on fire, causing damage in X's retail store. The defective wiring in the television was caused by an employee of Y who took unreasonable shortcuts in the soldering process. The employee knew that the method of soldering could result in the television short-circuiting if the unit overheated. In this situation X could sue Y for damages that occurred as a result of Y's negligent manufacturing process.

The Liability of the Designer in Negligence

A plaintiff who suffers injury or loss may also be able to recover damages from a product's designer, if the normal criteria for negligence are satisfied. It is conceivable that designers may design products which they know have the potential to be defective in certain foreseeable situations. If the designer does not tell anyone about this fault then he or she may be liable in negligence. However, it follows from applying negligence principles that designers are absolved from liability once they take all reasonable steps to avoid the occurrence of loss.

For example, a designer working to a fixed budget may realise that a product is defective in some circumstances. The designer may avoid liability by clearly explaining to the manufacturer the circumstances in which the product will be defective. The onus is then shifted to the manufacturer to take the necessary initiatives to correct the problem.

IV CRITICAL EVALUATION OF EXISTING PRODUCT LIABILITY PROVISIONS IN NEW ZEALAND

A Introduction

The previous section considered the product liability framework that currently operates in New Zealand. This part of the paper discusses the effectiveness of that framework in practice, identifying weaknesses that are present in New Zealand law. Dr Ellen Beerworth made the following comment in 1990. It would apply equally well to New Zealand today.

> The current body of law governing liability for products in Australia is a complex and disharmonious marriage of ancient and modern, and of judge-made and parliament-made rules. The complexity of this marriage stems from the fact that diverse contractual, tortious, and statutory rules operate concurrently. The disharmony in the marriage derives from the fact that these concurrently operating rules are in many ways inconsistent. Concerns of inequity and disadvantage, as well as concerns that undue complexity is wasteful of resources, prompted a review of the current Australian position in 1987.[67]

The findings of the Australian Law Reform Commission on product liability will be referred to in this part of the paper.[68] The pre-reform Australian regime was very similar to the current position in New Zealand. Policy makers in Australia concluded that the Australian law did not satisfy the policy goals of a successful product liability scheme.

B Liability for personal injury

Many of the potential holes in the cover under the ARCIA have not been tested in practice. In theory, it is clear that under the restrictive 1992 regime product liability cases are more likely than before to fall outside the cover of the ARCIA.

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67 Above n 19, 9.

68 Australian Law Reform Commission *Product Liability* Report No. 27 (Law Reform Commission, Sydney, 1988).

A recurring criticism of the ARCIA is that it no longer accords with the principle of real compensation that was first stated in the "Woodhouse" Report.[69] With the abolition of lump sum compensation and compensation for loss of enjoyment of life, many people are clamouring for the return of the right to sue which, they hope, would provide larger compensatory awards. Other groups are seeking to have the provision of accident compensation opened up to the private insurance market, in an attempt to increase competition and reduce administrative costs.[70] This possibility merits further scrutiny but is outside the scope of this paper.

Although cover under the ARCIA has been reduced by restricted definitions of key components such as "personal injury", in practice the Act will probably cover most product liability situations where personal injury or death result. Nevertheless, while the restrictive definitions remain in force, injuries will potentially fall outside the Act's cover. There is also a greater scope for victims of injury caused by defective products to bring actions for exemplary damages, encouraged by the chance of receiving a damages award to "top up" the ARCIA entitlement.

A comprehensive critical analysis of the accident compensation scheme is outside the scope of this paper. It is relevant to product liability that available compensation levels are severely reduced under the ARCIA. The way the premiums are levied does not provide a sufficient incentive for manufacturers to take the optimal level of care in the production of goods because premiums are imposed on employers with poor accident records, rather than manufacturers of defective goods. The current outcomes of the ARCIA therefore do not accord with the policy goals of a modern product liability scheme.

For example, a person injured by a defective product during the course of employment may be entitled to accident compensation under the ARCIA.[71] Although the employer may not be at

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69 Above n 13.

70 For example, the NZ Manufacturers Federation and NZ Employers Federation. See also the Reserve Bank Governor's comments about opening ACC up to competition in "Brash's ACC Medicine" *The Dominion*, 15 August 1996, 1.

71 The employer may also be subject to the provisions of the Health and Safety in Employment Act 1992, but we will assume that employer was not at fault in this example.

fault, the employer's ACC premium will be loaded to take into account the cost of all claims made by employees for injuries arising in the course of that employment. There is no incentive for the manufacturer to produce a safer product, because the employer bears the cost of the work-related injury.

Policy makers should consider the extent to which personal injury or death caused by defective products is likely to fall outside the cover of the ARCIA. If an injury does not fall within the cover of the ARCIA, then policy makers must consider whether any proposed legislation or other reform dealing with product liability should extend to such injuries.

C Liability for property damage

In practice, the various provisions governing consequential property damage are the most troublesome aspect of product liability law in New Zealand.

1 Consumer Guarantees Act 1993

Sections 18(4) and 27(1)(b) of the CGA impose strict liability on suppliers and manufacturers respectively where defective products have caused loss or damage to property.

These provisions do not require the claimant to prove fault by the manufacturer or supplier. They also allow claimants to recover damages from the manufacturer of the defective goods without being restricted by the lack of privity between themselves and the manufacturer. This is a significant step forward in providing adequate protection for persons who suffer loss.

However, in the product liability context, the CGA provisions arguably do not go far enough in protecting the rights of loss sufferers to receive efficient and effective compensation.

Sections 18(4) and 27(1)(b) are an *incidental* part of the CGA. They are not highlighted in such a way as to draw attention to the possibility of their application. They are contained in an Act that is concerned with the provision of post-sales guarantees.

Effective redress under the CGA in product liability situations is limited by the definition of "consumers".[72] This restriction means that the benefits of the strict liability provisions can only be reaped by those persons who have purchased or acquired the defective goods. The CGA will not provide a remedy for a person who suffers loss while using the consumer's goods, nor will it compensate an "innocent bystander" who suffers loss caused by the goods.

The CGA is one of New Zealand's main product liability vehicles, but it fails to address the situation where the loss sufferer does not "own" the defective goods. A person who is not a "consumer" as defined by the Act must rely either on contract law or negligence.

Article 9(b) of the EC Directive effectively limits claims for property damage to "consumers", but the Directive gives plaintiff's standing to sue on a different basis which does not rely on the injured person's "ownership" of the goods.

In the CGA, "consumers" are defined in relation to their status as the purchaser or "acquirer" of the goods which subsequently cause damage due to their defectiveness. Under the Directive a person can claim where defective goods cause damage to property ordinarily intended for private use or consumption. The restriction in the Directive arises from the nature of the property that is damaged, rather than the status of the claimant in relation to the goods that cause the damage.

This distinction is important. Under the CGA a person cannot claim for damage to property where that person is effectively not the owner of the goods that cause the damage. Under the Directive any person can claim for damage to property regardless of their title in relation to that property, provided that the damage being claimed for relates to goods ordinarily intended for private use.

2 *Contract Law*

Contract law may provide a remedy in situations where the definition of consumer means that the CGA does not apply. However, it will only apply to contractual relationships directly

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72 See above n 54.

between the seller and the purchaser of the defective goods. If for some reason a purchaser does not fall within the cover of the CGA, then the purchaser can only have a remedy against the person from whom he or she bought the goods. There will generally be no remedy against the manufacturer because there is no privity of contract. Similarly, there is no protection for the "innocent bystander", the subsequent purchaser, the donee or the lessee. The contractual remedy also turns on the seller's ability to meet the purchaser's claim.

As a policy option, the remedy is ineffective because it does not allocate the risk of loss to the person best able to prevent the loss. Most retailers will not even be aware of the steps involved in the production process and certainly will not be in a position to exercise any quality control over that process. Allowing the injured party to target the immediate seller for compensation provides only for compensating the victim. This produces a satisfactory result for the consumer but does not directly act as a deterrent to the manufacturer unless the seller brings a suit against the manufacturer. This can lead to a multiplicity of actions as suits follow down the chain of liability towards the party who was ultimately responsible for the defect. The chain may be broken by a contractual clause excluding liability, or by an insolvency.

This process is inefficient because it leads to greatly increased costs in the recovery process, which may result in inflated prices. In practice the contractual action will only be used by "commercial" consumers, who do not fall under the CGA.

3 Negligence

Where neither the CGA nor contract law apply, the negligence action is often the last resort of the loss sufferer. The law of negligence has many identifiable deficiencies in product liability cases:

- The person who suffers damage must generally prove fault by the manufacturer.[73] Without access to the manufacturing process this burden is difficult to satisfy in many cases. This situation is heavily weighted in favour of the producer and is a significant barrier to consumer redress in product liability cases.

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[73] See above n 63.

- The doctrine of *res ipsa loquitur* may be invoked in some cases, although its application is entirely at the Court's discretion. The entire doctrine is a matter of uncertainty in New Zealand therefore its usefulness is limited because of its unpredictability.[74]

- There is a high cost barrier involved in bringing a negligence action.

Proving a claim grounded in fault-based liability is far more costly and complex due to several factors: [75]

- To prove that the defendant breached a duty of care, the plaintiff must be fully informed about the defendant's manufacturing processes. This problem is made easier by procedures of discovery and interrogatories. A plaintiff can also obtain expert evidence in their favour, however this evidence can often be rebutted by expert witnesses with an opposing view. Expert witnesses are costly.

- It is often difficult to identify the act or omission which led to the production of a "defective" product. A manufacturer may avoid liability by establishing that the defect lay in a component part of the product. In this situation, the plaintiff must try to join the component manufacturer to the action, further increasing overall costs. Unless large sums of money are involved, consumers may be likely to give up before this stage in the process.

- Even if the act or omission can be identified, the plaintiff must prove that it constituted a breach of the duty of care owed to the plaintiff. Without knowledge of industry practice this will be difficult in most cases.

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74 See above n 63. 285.

75 Several of the following criticisms were put forward by the ALRC in their discussion paper on product liability reform in 1988. Above n 12, from page 12.

- Ultimately, due to cost barriers and practical barriers, the negligence action does not meet the policy goal of efficient and effective compensation, although in theory it has the potential to encourage optimal levels of care in production.

4 General criticisms

Multiple parties

In a contract or CGA action, the plaintiff can directly target the manufacturer or the supplier.[76] In a negligence action, the plaintiff may end up suing every identifiable person whose acts or omissions may have caused the goods to be defective. The plaintiff will have to consider joining the designer of the goods, a component manufacturer, a supplier of raw materials, a distributor and a retailer. This consumes the resources of the plaintiff, the courts and the potential defendants.

Inconsistencies in burden of proof

Liability in contract and under the CGA is strict. Liability in negligence is fault-based. The result is that the manufacturer's liability for producing a defective product that causes damage will be different depending on whether the person who suffered the loss is a "consumer" as defined in the CGA. Liability under the CGA or contract depends on the state of the goods. Liability in negligence depends on the conduct of the manufacturer. It is conceivable that one defective product could give rise to a CGA claim, a contract claim, a negligence claim or an ACC claim, depending on who was injured or suffered loss.

For example, if X buys a television which explodes due to a defect and damages property, then X has redress against the manufacturer in strict liability under the CGA. If X takes his television around to Y's house and the television explodes, damaging Y's property, the situation is different. X may claim against the manufacturer under the CGA for damage caused to Y's property. Y may not claim directly against the manufacturer under the CGA for the damage to her own property because the defective television did not belong to her.

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[76] Subject to privity considerations in the case of the contract action.

The liability of the manufacturer will vary depending on the relationship between the manufacturer and the person who suffers the loss. The relationship between the manufacturer of the goods and the person affected by those goods should be irrelevant in defining the manufacturer's liability for producing defective goods.

There is no logical reason why a person who suffers loss while using a product that he or she has purchased should get the benefit of strict liability, while the person standing next to them who also suffers loss must seek relief under the laws of negligence. This state of affairs simply highlights the haphazard approach by which this area of the law has developed.

D Conclusion

These criticisms demonstrate deficiencies in New Zealand's consumer protection framework that need to be corrected, as they were in Australia in 1992. The main problem is caused by requiring injured persons to resort to negligence actions where the CGA or contract law do not assist them. This does not equate with efficient and effective compensation for persons who suffer injury or loss. Why should a person who did not purchase or acquire the defective goods have to satisfy a different burden to someone who did purchase or acquire the defective goods?

Second, many of the existing provisions do not encourage manufacturers to take optimal levels of care in manufacturing their products. The lack of incentive is particularly apparent in the personal injury field due to the operation of the ARCIA. In the area of property damage, the CGA goes some way towards allowing the loss sufferer to directly target the manufacturer, but it is submitted that the CGA does not go far enough because of restrictions on the application of the Act.

The majority of the Tort and General Law Reform Committee (1974) considered the tendency in many cases for the manufacturer to settle in order to protect its commercial reputation and

advanced this as a reason for not reforming product liability law in New Zealand in 1974.[77] However, reliance should not be placed on a manufacturer's discretionary ability to settle a case out of court. This is not an adequate reason for retaining the current deficiencies in the law.

It is true that the main drive towards strict liability in the product liability arena has centred on personal injury claims.[78] Although the personal injury consequences of defective products are potentially more devastating, the protection of property should not be underplayed as an important aspect of law in New Zealand.

The Committee observed that claims for property damage caused by defective products in which the plaintiff does not obtain reasonable compensation are rare. A survey should be undertaken to determine whether this is still the case. It is possible that litigation is rare because the claimant either cannot afford to bring an action, or the chance of success does not match the investment of resources into the case. Even if claims of this kind are rare, it does not follow that current deficiencies in the law should not be remedied. While there exists a mere potential for injustices to occur, reform should be seriously considered. The current lack of rain is not a satisfactory reason for ignoring the hole in the roof.

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77 New Zealand Torts and General Law Reform Committee *Product Liability* (Ministry of Justice, 1974) 23.

78 This can be seen in the emphasis of the EC Directive on personal injury. Property damage in the Directive is given a more restricted scope. See above n 17.

V REFORM OPTIONS

A Important elements of Product Liability Systems

In my opinion, the following considerations should be taken into account when evaluating the effectiveness of any product liability framework.

- The system should not acts as a disincentive towards the production of goods using all reasonable care. A properly functioning product liability system should have a degree of deterrent effect against the production of defective goods, that will complement existing regulatory measures.

- Effective compensation should be one of the primary considerations of any product liability scheme. The scheme should allow the party who has suffered loss to seek an adequate remedy for that loss. This entails both efficiency in recovery without incurring unnecessary litigation costs, and adequate compensation for the loss suffered. The primary focus of the scheme should be compensatory.

- An effective product liability scheme should allocate the cost of losses caused by defective products to the party that is in the best position to bear the loss and take steps to prevent it.

- The framework should be internally consistent so as to avoid the situation where the same defective product gives rise to many different remedies and causes of action depending on the status of the injured person.

- The impact of the product liability scheme on international trade should be taken into account. The scheme should not adversely affect the flow of trade between countries, and should seek to enhance it as far as possible.

- Many power imbalances can be caused by the difficulties encountered in seeking compensation; the scheme should be relatively easy for the consumer to use, and should aim to address such imbalances.

B Statutory Strict Liability - The EC Directive and Australian Product Liability

1 Why are Overseas Developments Relevant to New Zealand?

The future direction of consumer policy in New Zealand need not be dictated by developments overseas, but policy makers should seek to benefit from overseas experiences. Harmonisation of consumer protection laws between trading partners is an effective way of breaking down barriers to international trade.

A key objective of CER (Closer Economic Relations) is to minimise trade barriers through harmonisation of laws. [79]

Australia enacted a new product liability regime in 1992.[80] The Australian regime was modelled closely on the EC Directive on product liability that was issued in 1985.[81] The Directive is a substantial step towards standardisation.

Under the terms of the Treaty of Rome, all the member States of the European Community (now the European Union) were required to implement the substance of the Directive into their domestic law. The EU is one of New Zealand's major trading partners. Now the influence of the Directive can be seen in domestic product liability laws in countries far beyond the borders of the EU itself.

Overseas developments are also valuable to New Zealand because they form a useful "testing ground" for policies that New Zealand could consider.

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79 CER is the trans-Tasman free trade agreement to which Australia and New Zealand are signatories. The harmonisation process is already well underway. An example of harmonisation of consumer laws is New Zealand's Fair Trading Act 1986. A conscious effort was made to draft this legislation using the Australian Trade Practices Act 1974 as a model.

80 Part VA of the Trade Practices Act 1974.

81 See above n 17.

2 *Background to the EC Directive*

In the late 1970s the Commission of the EC began to consider the issue of product liability reform with a view to issuing a Directive to member States. The principal motivation behind the Directive was a desire to achieve uniform product liability laws between the various member States, and a realisation that existing laws did not provide adequate compensation for consumers or adequate incentives for the production of safe goods.

The desire for uniformity was prompted by a concern over the protection of consumers and the barriers to international trade that could be presented by divergent domestic product liability laws.

Through issuing the Directive to all member States, the Commission enabled reform to occur on a uniform basis throughout Europe. The underlying philosophy of the Directive is stated in its preamble,

> Whereas liability without fault on the part of the manufacturer is the sole means of adequately solving the problem, peculiar to our age of increasing technicality, of a fair apportionment of the risks inherent in modern technological production.

3 *Application of the Directive*

The key principle outlined in Article 1 of the Directive is that manufacturers shall be liable without fault for damage caused by defects in their products. This is the principle of strict liability.

The Directive applies to all movable property.[82] Individual states have the option of applying the Directive to agricultural produce.

"Producer" is defined so as to include:

- A manufacturer of a finished product or component,[83]

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82 Article 2.

83 Article 3, para 1.

- Any person holding themselves out to be the manufacturer,[84]
- Importers of a product into the EC (without prejudice to the liability of the producer),[85]
- The supplier (if the supplier fails to divulge the identity of the manufacturer).[86]

4 Requirements for liability

Article 4 requires that the injured person must prove three things: damage, defectiveness of the goods, and a causal relationship between the defect and the damage.

Damage

"Damage" is defined in Article 9. The Article is prescribed without prejudice to national provisions relating to non-material damage.[87] Damage means personal injury and death, or damage to property other than the defective goods themselves. Pure economic loss does not appear to be covered under the Directive.

A limitation has been placed on an injured person's ability to claim for consequential damage to property. Claims are effectively limited to consumer goods, defined by reference to use and value.

The restriction on claims for property damage suggests that the primary focus of the Directive is on liability for causing personal injury.

Defect

Rights arise under the Directive where a damage-causing product is defective.[88]

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84 Article 3, para 1.

85 Article 3, para 2.

86 Article 3, para 3.

87 The effect of this proviso is that domestic laws relating to recovery of damages for pure economic loss will not be affected by the implementation of the Directive.

88 "Defective" is defined in Article 6.

A product is defective when it does not provide the safety which a person is entitled to expect, taking all circumstances into account, including:

(a) Presentation of the product;

(b) The use to which it could reasonably be expected that the product would be put;

(c) The time when the product was put into circulation.

(d) A product shall not be considered defective for the sole reason that a better product is subsequently put into circulation.

Whether a product is considered to be defective turns on the application of an objective test - what would the ordinary person expect?[89]

Defences

There are a number of limited defences to an action brought under the Directive:

It is a defence if the defendant proves that:

- the defendant did not put the product into circulation; or
- It was probable that the defect came into being after the goods were put into circulation; or
- The product was not manufactured for commercial purposes; or
- The defect was due to compliance of the product with mandatory legal requirements; or
- That the state of scientific or technical knowledge at the time the goods were put into circulation were not such as to allow the existence of the defect to be discovered (the "development risks" defence); or
- That the defect in a component is attributable to the design of the product in which the component has been fitted. This defence will exculpate a component manufacturer where a component part has been used in a design for which it is not entirely suitable.

The 'development risks' defence referred to above is the most controversial. Several States, including the United Kingdom would not have agreed to the Directive unless the defence was

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89 This objective test is similar to the test for "acceptable quality" of goods under the Consumer Guarantees Act. See section 7 of the Act.

included. The Directive allows members to decide whether to include this defence in their domestic law.[90]

This defence may arise more commonly in cases involving pharmaceuticals and chemicals. Such products may be placed on the market at a time when the state of scientific knowledge is insufficient to allow the discovery of a defect. The drug industry is often creating products for which the longterm effects may not be fully understood.[91]

Although the defence appears to give manufacturers a significant means of avoiding liability, the scope of the defence may be narrower than it first appears. For the defence to apply, the defect must not have been discoverable *at all* at the time of manufacture, rather than not being *reasonably* discoverable. This is an absolute standard.

The defence was allows into the Directive on the basis that denial of the defence would impose "liability both too extensive and unpredictable in scope, and might inhibit socially desirable innovation in the development of new products."[92]

The Directive also allows States to impose a limit on recoverable damages that arise as a result of a defect in a single product.[93]

5 *Significance of the Directive as an International Model for Reform*

The Directive allowed member States a period of three years in which to incorporate the Directive into their domestic law. France has yet to implement the Directive.[94]

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90 Luxembourg has included the defence.

91 The Dalkon Shield for example, the use of which could lead to sterility or even death.

92 D Harland "The Legal System on Product and Service Liability - The Australian Experience" Conference Paper, JASCA Conference, Kyoto, Japan, 1994.

93 Article 16.

94 Members of the EC at the time the Directive was issued were Belgium, Denmark, France, Germany, Spain, Ireland, Italy, Luxembourg, The Netherlands, Portugal and the United Kingdom.

As a result of the 1992 European Economic Area Agreement, six other European countries have implemented the Directives principles into their domestic law.[95] Other European countries have implemented the Directive while being under no obligation to do so, including Hungary, Switzerland and Russia.

The writer considers that the Directive has become the leading model for product liability reform in the western world. It embodies a worldwide belief that the future of product liability lies in a strict liability system. The influence of the Directive can also be seen in Israel, Brazil and the Philippines. Japan enacted the Product Liability Law of 1994 that is clearly modelled on the Directive. Australia has based its 1992 amendment to the Trade Practices Act 1974 on the Directive.

B Product Liability in Australia

1 Background to the Australian Reforms

Before 1992, the framework of laws governing product liability in Australia closely resembled the current provisions in New Zealand. Product liability actions were based on tort, contract and Part 2A of the Trade Practices Act 1974 which is essentially the same as New Zealand's Consumer Guarantees Act 1993.

Although liability of the manufacturer for damage caused by defective products is strict under Part 2A of the Trade Practices Act, recovery is limited to consumers as defined under that Act. A person who does not purchase or acquire the defective product cannot seek damages under the Act.[96] The possibility of recovering damages for personal injury or property damage is an incidental part of the legislation rather than a major focus.

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95 Austria, Finland, Iceland, Liechtenstein, Norway and Sweden. Austria, Finland and Sweden joined the EU on 1 January 1995.

96 Section 4B of the Trade Practices Act 1974.

In 1987 the National Consumer Affairs Advisory Council recommended that a comprehensive study be undertaken to determine the adequacy of existing remedies and examine the viability of enacting a form of strict product liability. The Australian Law Reform Commission published its report in 1988,[97] concluding that reform was clearly necessary for reasons of consumer policy and economic efficiency.

The ALRC argued for a radical form of manufacturer's liability that turned on whether a product caused injury. The recommendations departed from the EC Directive by removing the need for a plaintiff to show that a product was defective. The claimant would only be required to show a causal link between the behaviour of the product and the injury. The Committee considered that the test for defectiveness as outlined in the Directive would lead to the same unpredictable outcomes that have resulted from the use of the "reasonable care" test in the law of negligence.

The ALRC recommended that manufacturers and suppliers of goods should be liable for loss caused by those goods if the loss was caused by the way the goods acted. The plaintiff would not need to focus on whether the goods failed to comply with some standard of safety or quality, which many commentators saw as inviting the courts to balance risks and benefits in a similar way to the law of negligence.[98] Harland notes that under the new product liability law in Australia, courts will "often in effect be asked to decide what level of safety is socially acceptable in our community for this type of product, given that absolute safety is unattainable."[99]

The report prompted extensive debate. Industry sectors in Australia considered that the proposed focus on causation alone would impose too heavy a burden on manufacturers.[100] The federal government saw the ALRC's radical reform as being too hard on producers. This

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97 Above n 19.

98 See for example J Stapleton "Products liability reform - real or illusory" (1986) 6 Oxford Journal of Legal Studies 392.

99 D Harland "The Legal System on product and Service Liability - the Australian Experience" Conference Paper, JASCA Conference, Kyoto, Japan, August 1994, 6.

100 Commonwealth of Australia, Industry Commission *Product Liability* Report No.51, 1989.

form of the proposal was not adopted. Instead the federal government chose to follow the model provided by the EC Directive as a compromise solution.

2 Why did the ALRC recommend reform?

The ALRC measured the existing state of product liability provisions in Australia against three benchmarks to determine whether the existing law was performing satisfactorily. The following paragraphs will examine some of the ALRC's findings. This section will simply illustrate the types of finding that were made:

Policy Grounds

(a) The law must ensure that those who manufacture and supply goods - and their customers - bear the risk of losses caused by what the goods do.[101]

The ALRC found that the Australian law failed to match the 'risks' with the benefits for six independent reasons.[102] For example, the existing law drew a distinction between classes of people who suffer loss. The law regarded a buyer differently to a non-buyer in situations where goods caused damage or injury. Second, it may be impossible to identify the party who is responsible for what the goods did. Third, the measure of damages differed depending on the cause of action pleaded, which does not necessarily bear any rational relation to the loss suffered by the claimant

(b) The law should properly take account of other factors involved in the occurrence of losses

The ALRC found that the existing law failed to meet this policy objective in most cases. The conduct of the claimant, which may have contributed to the loss, was not sufficiently emphasised in the existing law.

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101 This standard and those that follow are taken from the ALRC report, above n 68, 35-36.

102 Three of these reasons will be mentioned in this paper.

(c) The law should minimise the cost of recovery

The ALRC found that transaction costs relating to the existing causes of action, especially negligence, were high.

Economic Efficiency

The main criticism in this area was that the existing law relied too heavily on vague standards. The ALRC suggested that this vagueness would generally produce inefficient allocation of resources by persons involved in the manufacture and supply of goods, which would lead to price distortions.

Empirical Evidence

Although there was some debate over the quality of the evidence produced, the ALRC concluded that there was some cause for concern about:

- The number of injuries and deaths caused by goods
- The degree to which several aspects of the existing law presented a barrier to the enforcement of the rights that it conferred.

By matching the existing law against the three standards above, the ALRC identified unacceptable inadequacies in Australia's existing law and established a clear need for reform.

4 The Reform

Part VA of the Trade Practices Act 1974 came into force on 9 July 1992. The amendment contains the product liability reforms eventually decided upon by the Australian government.

5 *How has Australia implemented the Directive?*

The provisions of the TPA relating to the form of liability, interpretation of defect and damage, and the defences do not depart from those in the Directive. Australia has included the "development risks" defence in their legislation.

There is a limitation period of three years from the time the plaintiff became aware or ought reasonably to have become aware of the loss, the defect and the identity of the manufacturer.

Also in accordance with the Directive is the "statute of repose" provision, which extinguishes the cause of action if action is not commenced within 10 years from the time of the supply by the manufacturer of the actual goods that caused the injury. This provision is also controversial, as in some cases, especially pharmaceutical cases, the damaging effects of the product may not be felt until after the 10 year period has expired.

C *New Zealand's Trading Partners*[103]

It is important to consider the product liability schemes that have been adopted by New Zealand's main trading partners. The EC Directive and the reforms in Australia aimed to reduce barriers to international trade. Through the adoption of laws that are consistent with the laws of their trading partners, countries can reduce barriers to trade between each other.

1 *Australia*

Australia is New Zealand's largest trading partner. Due to CER, New Zealand has a positive obligation to take steps to remove barriers to trade between the two countries. Australia has adopted a strict product liability regime in the form discussed above.

2 *Japan*

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103 According to statistics obtained from Statistics New Zealand, for the year ending August 1995, New Zealand's top five trading partners are, (in descending order of amount of trade conducted in monetary terms), Australia, Japan, United States of America, United Kingdom and Germany.

New Zealand is trading increasingly with Japan. In 1994, Japan enacted a product liability law that imposes strict liability on manufacturers of defective products. The Product Liability Law of 1994 is modelled closely on the EC Directive.

3 *United States*[104]

New Zealand still conducts a large amount of its trade with the United States. Product liability in the United States is a subset of tort law. It operates on strict liability principles - a plaintiff is not require to prove fault by a manufacturer if the product is defective in the sense of being "unreasonably dangerous". However, certain legal structures and principles mean that the United States has a unique way of dealing with product liability claims.[105] Factors affecting the process include; the role of the jury, court procedures, different approach of courts to the application of precedent and to certainty and predictability in the law.

4 *Europe*

New Zealand conducts a large amount of trade with the EU. All the EU countries except France have now implemented the Directive into their domestic law.[106]

5 *Conclusion*

All of New Zealand's major trading partners operate in accordance with a strict liability system of product liability. At present New Zealand does not have such a scheme. An analysis of the economic effects of this difference is beyond the scope of this paper. Policy makers should consider the extent to which, if at all, trade with New Zealand's major trading partners might be enhanced by enacting some form of strict liability scheme in New Zealand.

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104 The United States' approach to product liability cannot be accurately explained within the constraints of this paper. For a brief summary of the US system, see For further reading on comparative product liability laws see generally CJ Miller (ed) *Comparative Product Liability* (British Institute of International Comparative Law, London, 1986) and G Howells and JJ Phillips (eds) *Product Liability* (Barry Rose, Chichester, 1991). See also G Howells *Comparative Product Liability* (Dartmouth, Aldershot, 1993).

105 This statement about the law in the United States is taken from Beerworth's book, above n 19.

106 For a list of the countries who are members of the European Union, see above n 94 and 95.

D Consideration of Directive - based Liability

Advantages

- Modern methods of production and distribution impose an unfair burden on injured persons in requiring them to prove negligence against a manufacturer. Fault liability is recognised as a costly and inefficient means by which to seeks redress.

- Individuals in the current economic climate are more likely to under insure themselves that manufacturers. It is unfair to put the onerous on individuals to insure themselves against loss, which can have a devastating effect on the individual. Personal insurance also provides less of an incentive for manufacturers to improve their system. It is better for the cost of defects to be spread around all consumers through increased pricing due to increased premiums paid by manufacturers.

- Considering the insurance aspects of strict liability, the practical effect of manufacturers taking out insurance will act as a deterrent, as consumers will tend towards a cheaper, more effective product. Insurance companies should increase premiums or refuse to extend cover to a company with a bad record. This will also act as a deterrent.

- There is a moral obligation which dictates that responsibility for a defective product should lie with the manufacturer of those products, because they are in the best position to prevent the defect.

- Strict liability (in a statutory form) may discourage litigation, which means that there may be more settlements as it will be clearer whether the manufacturer is liable.

- Some would argue that the way "defectiveness" will be interpreted under a Directive-based scheme does not differ greatly from the cost/benefit analysis applied under negligence law. However this argument applies more readily to design defects than manufacturing defects.

  Manufacturing defects, being inadvertent, will be effectively assessed against the manufacturer's own standards, and therefore will be found to be defective even though there may be no actual negligence involved. This is an advantage to the consumer.

In spite of the criticisms of the "defectiveness" concept, the situation in respect of design defects will be no worse than the existing negligence law, and it may be substantially easier for the consumer to receive effective compensation.

Disadvantages

- Manufacturers would inevitably incorporate insurance costs into the price of the product, thus resulting in increased cost which would be passed on to consumers. This might be detrimental to the consuming public as a whole. This may also result in New Zealand products becoming less competitive in the international market.
- The manufacturer may be held liable for marketing and design defects which are not within the ambit of the manufacturer's control.
- Under a Directive model, manufacturers appears to have no positive obligation to order a product recall once they become aware of a defect.

E Implementation Options for Statutory Strict liability

The discussion above has centred around a statutory form of strict liability as a viable option for product liability reform in New Zealand. If this type of reform were adopted, the key question is whether product liability deserves its own statute, or whether product liability amendments could be annexed to an existing statute.

1 A Self-Contained Product Liability Law

Japan opted for a discrete product liability statute. Codifying product liability law into one statute would lend clarity to the end result. The target users of the law (being the consuming public as a whole) would more easily understand what that law was about, which would make the law more accessible. It would be possible to take Part VA of the Trade Practices Act (Australia) and translate it into the New Zealand situation under a single statute. This is an option which should be seriously considered.[107]

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107 This paper has only provided the reader with the "bare bones" of the Australian scheme. For a more detailed analysis of Part VA, readers should refer to Beerworth, above n 19.

One of the major issues facing New Zealand product liability law is that standing to sue under the CGA is limited to those who exercise some form of ownership over the defective product. Adopting the terms of the Directive would give standing to a class of people who are likely to suffer product-related loss or damage, eliminating the practical inconsistencies caused by the drafting of the CGA.

While personal injury is largely covered under the ARCIA, a policy issue is whether a separate statute is warranted. I believe that it is, although the personal injury side to the legislation would be subject to the ARCIA, in particular section 14. The existence of the new product liability law should not preclude the consumer from pursuing other available remedies.

2 *Product liability under an Existing Statute*

It would be possible for New Zealand to enact an amendment to one of our existing statutes to incorporate the EC model of strict liability. The two possible candidates for amendment are the Fair Trading Act 1986 and the Consumer Guarantees Act 1993.

The CGA already deals with product liability to some extent therefore some would argue that it could simply be extended to include the provisions of the EC Directive. However, under the current provisions of the CGA, relief is limited to consumers, as defined in the Act and discussed above. To properly introduce strict liability as under the EC Directive, an amendment to the CGA would require the use of a broader definition of "consumer".

The existing definition of consumer is appropriate for the CGA because it provides guarantees and remedies to those who have "acquired" the goods. This is entirely appropriate in the context of an Act which is designed to give remedies to consumers of goods and services where the goods or services do not meet a certain standard. As discussed earlier, product liability does not focus on the relationship between the manufacturer and consumer so much as the effect of the defective product on the consumer. Bearing this in mind, effective implementation of the EC Directive would require a wider definition of "consumer" to be

used in the part of the Act which dealt with product liability. The use of two definitions of "consumer" in the same Act would lead to unnecessary confusion.
Consequently it is submitted that the CGA is not a suitable vehicle for product liability reform.

The Fair Trading Act ("FTA") may accommodate product liability amendments more comfortably. If a distinct product liability Act were unsuitable for New Zealand conditions, then an amendment to the FTA could be considered.

The FTA already deals with issues of product safety regulation under Part III. It would be possible to simply add another Part to deal with product liability, avoiding the confusion that would result from amending the CGA.

F Extension of Tort Law

1 Res Ipsa Loquitur

From the injured plaintiff's point of view, one of the most onerous aspects of negligence as a cause of action is the burden of proof which requires the plaintiff to prove that the manufacturer (or some other party) was at fault.

If the negligence action is to be useful in the product liability context, then codification of *res ipsa loquitur* should be considered. If codification is not possible then clear judicial guidelines should be set down at Court of Appeal level. *Res ipsa loquitur* has potential to ease some of the difficulties encountered by plaintiffs when bringing a negligence action, but at present it is perhaps too discretionary and unpredictable to be relied on by plaintiffs in product liability cases.
The Torts and General Law Reform Committee (1974) considered that this doctrine could ease some of the harshness consumers faced under existing law.[108] Referring to the adoption of

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108 Above n 77.

strict liability rather than use of *res ipsa loquitur* the minority considered that "it is preferable as a matter of principle to adopt openly, directly and consistently a rule that comes close to being achieved in practice anyway."[109]

Ultimately the clarification of *res ipsa loquitur* as a solution would be a satisfactory stop-gap measure, perhaps if personal injury compensation reform was imminent. As a long term solution the proposal does not address the existing problems with consistency between remedies.

As an additional cautionary note, Beerworth comments ,

> Our society should not lose sight of the fact that the casting of the burden of proof onto plaintiffs acts as a safeguard in the administration of justice, and that the burden is only ever reversed in very limited and discrete circumstances. In our rush to compensate consumers suffering product-related loss or damage, our society should also not assume that justice is the sole prerogative of consumers."[110]

2 *The United States Approach*

Instead of enacting product liability legislation, the United States legislature married concepts of "unreasonable danger" and defectiveness together into S402A of the Restatement (Second) of Torts. Liability will arise where a product is in a "defective condition unreasonably dangerous" to persons and subsequently causes harm.

As indicated by Clark,[111] these four words have led courts in the United States to a variety of views about the criteria for liability, which has caused considerable problems and resulted in a mass of literature on the subject. The lack of statutory guidelines appears to have caused the courts to have divergent views on the conceptual basis of defectiveness.

The United States version of product liability would appear to be more flexible, but flexibility often pairs itself with a degree of uncertainty. Uncertainty is a feature of existing negligence law

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109 Above n 77.

110 Above n 19, 33.

111 A Clark "The Conceptual Basis of Product Liability" (1985) Mod L Rev 325.

which could be avoided by a statutory model for liability. Consumers should (and arguably have a right to) understand law which protects them. It is difficult to see how this could be achieved other than by using a statutory model.

G Compulsory Insurance

Some commentators may suggest that the predominance of house and contents insurance in New Zealand today means that from a practical perspective, product liability involving property damage cases will more than likely be covered by the individual's insurance rather than proceeding to a formal action through the courts.

In particular, this view was adopted by the majority of the Torts and General Law Reform Committee (1974) in its report on product liability.[112] The Committee considered the possibility of introducing strict liability into the law governing product liability cases in New Zealand. The majority of the Committee concluded that modification of the law governing product liability in New Zealand at that time was not necessary.

> In light of the widespread practice of insuring there is good administrative reason for allocating the costs of any property damage to the insured individual. Payment from his own insurance company is likely to be quicker than payment by the manufacturer's insurer. In the latter case the loss has to be investigated by two insurance companies involving duplication of work and extra cost.[113]

This reasoning assumes that personal insurance covering property damage is widespread, and adequate to meet the cost of the loss. In the current economic climate it is doubtful that all people will be able to insure themselves adequately, if at all, against loss of this kind. The minority of the Committee recognised this point.[114]

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112 Above n 77.

113 Above n 77, 22.

114 Above n 77, 24.

The majority also considered that "there is good administrative reason for allocating the costs of any property damage to the insured individual."[115] The policy assumption behind this conclusion suggests that people are effectively obliged to insure themselves against the loss because the administrative costs will be reduced. Consequently, if individuals fail to insure themselves, the law may not be able to provide a satisfactory remedy. The minority of the Committee stated that "it is wrong in principle to restrict the manufacturer's liability on the assumption that consumers will be covered by insurance that they are under no obligation to carry." It is submitted consumers generally should not be required to take out insurance policies simply because the law fails to provide an adequate remedy.

A further disadvantage with personal insurance as a means of providing remedies in product liability situations is that manufacturers have less incentive to produce safe goods because they will not often be directly liable to compensate the injured person. They may be forced to account to the insurer under subrogation principles, but unless the claim is large the current state of the law means that the insurer may not bother to bring the claim at all. The policy goal of effective compensation may be satisfied, but only at great personal expense to the consumer in the form of insurance premiums. Secondly, the policy goal of deterrence is remains largely unsatisfied.

H Subrogation under the ARCIA

Some commentators may argue that we should allow the ACC to take up the common law rights of injured persons as against negligent manufacturer under subrogation principles, as if they were insurers.

Under such a mechanism, ACC would have the power under the ARCIA to adopt the injured person's right to sue a negligent manufacturer/importer/designer. This would allow the ACC to recover the cost of compensation that has been paid out to the injured person.

Unfortunately this proposition has three major flaws. First, under the ARCIA as it stands presently the injured person would be no better off than they are now unless the difference between the damages awarded by the court and the compensation that was paid out under the ARCIA was

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115 Above n 77, 22.

forwarded to the injured person. How would the ACC choose which cases to take to court? Extra compensation would depend on ACC's discretion to take further action against the negligent party.

Second, even if this was done, allowing the ACC to sue would mark a return to the inefficiencies of the pre-1972 system, which the accident compensation scheme intended to eliminate.

Third, allowing the ACC to sue using the current law does not alleviate any of the difficulties that are encountered when suing under the current law. Ultimately the extra costs of administering this amendment would be passed on to those who fund the scheme - the taxpayer, employers and motorists.

I Dispute Resolution Procedure

Product liability claims tend to pit individual consumers against manufacturers, who are generally larger commercial entities having more cash with which to defend an action. Litigation itself presents a barrier to effective redress in consumer cases. Consumers often resign themselves to the fact that the overall costs in time and money that are involved in bringing an action render it unrealistic.

In my opinion, while reform of the product liability laws will be a significant step in the right direction, practical implementation of any consumer law is difficult under the current judicial system because it is simply too daunting. The use of the Disputes Tribunal goes some way towards alleviating this difficulty but its jurisdiction is limited to claims involving $3000 or less, or $5000 by agreement between the parties.

A prescribed disputes resolution procedure would be a useful addition to any reform in this area. I propose implementation in the following way.

The consumer who suffers loss may elect whether to litigate in the courts or go through an alternative dispute resolution process. Under the second option, once the consumer has commenced proceedings, the consumer and the manufacturer would go through a compulsory mediation process with a Court appointed mediator.

This arrangement has the advantage of cutting down the procedural barrier to effective redress, and would result in a more accessible process that has the potential to produce equitable results. There is a possibility that the defendant would not be willing to put sufficient effort into mediation. However, the mediation would serve at least to clarify the issues and hopefully reduce the cost of any ensuing litigation. This process is a realistic alternative because it may achieve compensation where the consumer would otherwise be "litigated" out of effective redress.

At any stage in the process, the consumer would have the option of backing out of the process and litigating in the normal fashion.

VI CONCLUSIONS

Being realistic, product liability law in New Zealand is not in a state of turmoil that requires immediate legislative action. However, as I have suggested earlier in the paper, must we wait until the deficiencies in the existing law manifest themselves in such a way that they can no longer be ignored?

There is a need for reform in this area. Overall, the existing means of seeking redress fall short of providing effective compensation and encouraging optimal levels of risk prevention.

On balancing the policy considerations, I would advocate legislative reform as the most effective means of bringing New Zealand's product liability law up to the standard that has been set in other parts of the world. In my view, there are two options which best satisfy the policy goals that have been discussed in this paper.

First, a strict liability system based on the Australian model is the most preferable option. However, while New Zealand still has the ARCIA, any new statute would be subject to the ARCIA where personal injury was caused. This may mean that in practice, the personal injury provisions of the new statute may be under-used, but they will still be of benefit where the ARCIA does not apply.

Second, Parliament could extend the FTA to take into account strict liability provisions dealing with property damage that are modelled on the Directive/Australian legislation.

Whichever option is chosen, the benefit to be gained is a law governing product liability that is codified into one statute, thereby reducing uncertainty and providing a consistent remedy for those who suffer injury or loss caused by defective products.

Such a reform is not likely to be popular with the manufacturing and industry sectors. It would nevertheless be a significant step towards empowering consumers by minimising the effect of power imbalances caused by the existing law.

In the future, consumers are less likely to understand the technology that governs their daily lives than they are presently. Policy makers should be proactive rather than reactive in affording protection to the rights of consumers.

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