SUPREME COURT OF QUEENSLAND

CITATION:	*Ansell Ltd v Coco* [2004] QCA 213
PARTIES:	**ANSELL LIMITED** ACN 004 085 330 (plaintiff/respondent) **v** **SANTO ANTONIO COCO** (defendant/appellant)
FILE NO/S:	Appeal No 372 of 2004 DC No 94 of 2003
DIVISION:	Court of Appeal
PROCEEDING:	General Civil Appeal
ORIGINATING COURT:	District Court at Brisbane
DELIVERED ON:	25 June 2004
DELIVERED AT:	Brisbane
HEARING DATE:	27 May 2004
JUDGES:	McMurdo P, Williams JA and Chesterman J Separate reasons for judgment of each member of the Court, each concurring as to the order made
ORDER:	**Appeal dismissed with costs to be assessed on an indemnity basis**
CATCHWORDS:	GUARANTEE AND INDEMNITY – THE CONTRACT OF GUARANTEE – RIGHTS OF SURETY – AGAINST PRINCIPAL DEBTOR – where rubber roller supplied to company under contract between respondent and company – where appellant was director of company and provided guarantee for payment of all debts and monetary liabilities owed to respondent by company – where company had gone into liquidation before litigation was commenced – where respondent claimed for moneys owed under contract – where appellant counter-claimed at trial that company had a claim for breach of warranty against respondent and sought to set off quantum of damages recoverable against appellant's liability under guarantee – where learned trial judge found that appellant had not established breach of warranty – whether appellant could by way of defence rely on asserted claim by principal debtor against creditor for unliquidated damages for breach of warranty – whether breach of warranty established CONTRACTS – GENERAL CONCTRACTUAL PRINCIPLES – CONSIDERATION – FAILURE OF

CONSIDERATION – where company used roller purchased under contract for 23 days before noticing some malfunction and continued to use roller for 24 to 48 hours after that – where company did not pay amount due under contract – whether total failure of consideration – whether company indebted for amount under contract

Alcoy and Gandia Railway and Harbour Co v Greenhill (1897) 76 LT 542, cited
Cellulose Products Pty Ltd v Truda (1970) 92 WN (NSW) 561, cited
Covino v Bandag Manufacturing Pty Ltd [1983] 1 NSWLR 237, cited
Indrisie v General Credits Ltd [1985] VR 251, cited
Langford Concrete Pty Ltd v Finlay [1978] 1 NSWLR 14, considered

COUNSEL: A N S Skoien for the appellant
J A Logan RFD SC, with P A Looney, for the respondent

SOLICITORS: Gilshenan & Luton for the appellant
Forbes Dowling for the respondent

[1] **McMURDO P:** I agree with Williams JA's reasons for concluding that on the evidence the learned primary judge was entitled to find that Mr Coco did not demonstrate that the consideration for the purchase of the recovering of the suction press roll from the respondent wholly failed, nor that the roll failed because of the respondent's breach of warranty.

[2] Counsel for Mr Coco, in support of his contentions, emphasised the correspondence between the parties, or those associated with them, after the suction press roll failed. On 24 July 2001, the respondent wrote to the managing director of Softex Industries Pty Ltd ("Softex"), Mr Morris, requesting payment of an account which included a claim for recovering the suction press roll, noting: "To my knowledge, no formal written reason for non-payment has been received to date." Mr Coco, on behalf of Softex replied in these terms:

> "The Roll Press failed as it De-Laminated. We asked that your Manager attend our premises. A Mr Val Faoro visited our premises and after inspection and discussion I asked him to write to me and as of today's date I have still not received any correspondence – hence the delay in writing to you. For this I apologise."

[3] Mr Faoro replied by letter of 29 August 2001 to the effect that the failure of suction press rolls at other locations had been caused by chemicals and enquiring whether listed chemicals were used in Softex's manufacturing process. The undisputed evidence at trial was that Softex did not use these chemicals.

[4] On 29 November 2001, Mr Morris on behalf of Softex wrote to the respondent about a quote they had supplied for a blind drill press roll, expressing concerns about the warranty offered because of Softex's dispute about the de-bonding of the roll cover on the suction press roll and asking "to confirm your warranty concerning the lifting and quality of the roll cover and if any improvement has been made in the bonding of the Roll Cover to the Shell".

[5] Mr Faoro replied as follows:

"Further to our telephone discussion today, I can confirm that we have reviewed all of our manufacturing procedures on the sale of the business to Rapid Pacific Roll Covering Pty. Ltd.

We have also had an investigation by our principals, Stowe Woodward of the USA, and we currently have one of their technical managers here at our Melbourne plant. A thorough investigation of our materials and processes has been completed and our investigation focused on the following:-

- A re-evaluation of all materials and compounds used in roll covering. This included a review of the materials and the method of testing our compounds and compared these to Stowe Woodward USA. This has found that we have no discrepancy in either the compound and/or materials used.
- A review of all practices affecting bonding against our Standard Operating Procedures (SOP). This included the following:-

  . Cleaning of all metal shells prior to the application of primer.
  . The correct application of both primers and cement, including viscosity and percent dilution.
  . Use and application of primers and cement within the designated time frame to ensure their correct chemical cross bonding and adhesion.
  . The procedures for the application of the base, tie-in and cover to the shell.
  . The curing process, including a review of autoclave temperatures, length of cure and preheating to achieve the correct cross linking of the polymers to the metal of the shell.

Following this review we have screened and upgraded our shot blasting and metal preparation facilities where we are using a shot size and type that leaves little residue and maintains a much higher level of surface cleanliness after shot blasting.

As a further safeguard we have introduced the step of cleaning the shot blasted surface with a solvent to remove any possible debris or contamination.

The shot blasting unit will have the shot replaced more frequently and shot screened to a more precise size distribution.

Similar rolls to yours have recently been recovered for Carter Holt Harvey Tissue and also Austissue in Queensland and confirmation of bond integrity has been received and we do not believe that bond separation should be of concern in future recovers done at our plant."

[6] This correspondence did not require the primary judge to reject the evidence of Mr Faoro that the roll cover on the suction press roll had not debonded or delaminated. The assurances were given in the context of encouraging Softex to purchase a blind drill press roll and need not have been considered as an admission against interest as to the reason for the failure of the roll cover on the suction press roll the previous June.

[7] Because the appeal fails on the grounds raised, it is unnecessary to consider whether Mr Coco, as guarantor of the debt of Softex (now insolvent) to the respondent, could raise Softex's claim for damages for breach of warranty as a defence to the action against him on the guarantee without joining Softex as a party.

[8] The appeal should be dismissed with costs to be assessed on an indemnity basis.

[9] **WILLIAMS JA:** The appellant, who was the plaintiff in the proceedings in the District Court, appeals against the judgment in favour of the respondent (the plaintiff at trial) for $73,754.58 with interest accruing at $16.20 per day from 20 December 2003 and consequential orders. The respondent sued on a guarantee given by the appellant dated 28 August 2000. In his defence, as amended, the appellant raised a number of issues, including an allegation that for a number of reasons the guarantee was not enforceable against him. The appellant did not give evidence at trial and issues such as the enforceability of the guarantee appear not to have been seriously litigated. The learned trial judge concluded that the "defence concerning the alleged invalidity and unenforceability of the guarantee and of the charge fails as does the allegation that the purchases of the roll cover and the stofoil were not made on the credit account"; there is no appeal from those findings.

[10] As will be clarified later the defence at trial essentially litigated two issues and they were the issues that were the subject of submissions on the hearing of the appeal.

[11] At all material times the appellant was the sole director (and managing director) of a company Softex Industries Pty Ltd ("Softex") which was a manufacturer of paper products.

[12] The respondent, which relevantly traded under the business name "Dunlop Duratray" was a supplier, inter alia, of rubber roll coverings for rollers used in the pulp and paper industry in Australia.

[13] In August 2000 Softex applied to the respondent to open a credit account covering the supply of product by the respondent to Softex. As part of that application the appellant executed a form of guarantee and indemnity guaranteeing "the payment of all debts and monetary liabilities of the Customer which may from time to time be owing by the Customer to Dunlop Duratray ('the Debt') and undertake to repay on demand by Dunlop Duratray any part of the Debt if the Customer does not pay it when due."

[14] At the request of Softex the respondent submitted in January 2001 a quotation for the recovering of one of the rollers used in the factory of Softex in accordance with certain specifications provided by Softex. That quotation contained a warranty in the following terms:

> "Because of so many conditions existing beyond the control of Dunlop Duratray in the use of roll coverings, no warranty as to life or length of service is made. All roll coverings are warranted to be free

> of defects in material and workmanship. No claim will be honoured or adjustment made on any roll covering after one year from date of invoice or shipment.
>
> Our liability for breach of warranty is limited to the replacement of the roll covering. Consequential damages are not allowed."

[15] The quotation was accepted and in February–March 2001 the respondent carried out the necessary work in providing a new rubber coating for the appellant's roller. On completion of the work the recovered roller was delivered to Softex on or about 20 March 2001.

[16] The invoice issued by the respondent for supplying the new rubber coating was $56,903.00. In addition to that in the month of March a product known as Stofoil was provided at a cost of $774.40. That made the total indebtedness of Softex to the respondent $57,677.40.

[17] Softex installed the recovered roller in its plant and used it for some 23 days. On or about 6 June some malfunction was noted (unusual vibrations), but the management of Softex made the deliberate decision to continue operations with the roller. That continued until the roll was effectively destroyed on 8 June 2001.

[18] At trial it was conceded that Softex had not paid the $57,677.40 claimed by the respondent. In evidence it was said that Softex went into administration on or about 5 October 2001, and it was admitted in the pleadings that at the time the litigation was commenced Softex had gone into liquidation.

[19] As already noted there were two issues primarily litigated at trial and agitated again on appeal. Firstly, it was claimed that the consideration for the purchase of the recovered roller ($56,903.00) wholly failed. In consequence it was said that there was no indebtedness on the part of Softex in that sum. Secondly, it was asserted that Softex had a claim for breach of warranty against the respondent which the appellant then raised by way of counter-claim in the proceeding and he sought to set off the quantum of damages so recoverable against his liability under the guarantee.

[20] The learned trial judge concluded that "the allegation of there being a total failure of consideration fails." In arriving at that conclusion the learned trial judge noted that the roller "had been used 24 hours a day for some 23 days" which suggested that when "put into service it was not defective and that the problems developed subsequently." He then expressly referred to the fact that the roller was used for some 24 to 48 hours after problems were first noted. If the machinery had been stopped when that vibration was first noted the problem may have been able to be remedied.

[21] The fact that after the initial problem was noted the roller was used until its effectiveness was totally destroyed means that Softex could not establish that there had been total failure of consideration. Indeed counsel for the appellant did not press his submissions in that regard.

[22] On the hearing of the appeal members of the court raised with counsel (both for the appellant and respondent) whether a guarantor could by way of defence rely upon an asserted claim by the principal debtor against the creditor for unliquidated damages for breach of warranty. Neither counsel was in a position to refer the court

to any relevant authority. Senior counsel for the respondent submitted that it was "a moot point" but did not expressly submit that the "defence" as pleaded was misconceived.

[23] The question is discussed at page 545 and following of O'Donovan and Phillips, *The Modern Contract of Guarantee* (3rd edition). The position in Australia appears to be that, where a solvent principal debtor's claim against the creditor is for unliquidated damages in respect of the guaranteed transaction, the guarantor cannot plead the claim as a defence to an action on the guarantee if the principal is not joined as a party to the proceedings. That statement at 548 of the textbook is clearly based on the decisions in *Cellulose Products Pty Ltd v Truda* (1970) 92 WN (NSW) 561, *Covino v Bandag Manufacturing Pty Ltd* [1983] 1 NSWLR 237, and *Indrisie v General Credits Ltd* (1985) VR 251. The Victorian Full Court in the latter case, referring to the earlier New South Wales decisions, said at 253 that "a guarantor under a guarantee which makes him liable without more for the full indebtedness of the debtor for goods supplied cannot rely upon a cross-claim for damages which may be available to the principal debtor as against the creditor in reduction of, or as a defence to, his liability under the guarantee." In *Cellulose Products* at 588 Isaacs J indicated the procedure which should be followed in such circumstances:

> "This review of the cases lends no support to the submission that a surety when sued is entitled to set up in equity or at law as a equitable plea any cross action for unliquidated damages which the debtor may have against the creditor in respect of the transaction, the performance of which the guarantor had entered upon his guarantee; that is, in the absence of the debtor being before the court in the proceeding so as to be bound by verdict and judgments. This of course does not mean that the guarantor is without remedy; when he is sued he has a right immediately to join the debtor as a third party and claim complete indemnity from him. The debtor has then a right to join the plaintiff as a fourth party, claiming damages for breach of warranty and so obtain indemnity either in whole or in part. All the actions would be heard together, the rights of all persons determined and appropriate set-off's made after verdict, and if there be any surplus of damages over and above that which is required to meet the guarantee, the debtor will have recovered that from the creditor who, in the result, will get no more than that to which he would be justly entitled."

[24] But what of the situation where, as is the case here, the principal debtor is insolvent? After referring to a statement by Stirling J at 553 in *Alcoy and Gandia Railway and Harbour Co v Greenhill* (1897) 76 LT 542, Isaacs at 585 in *Cellulose* noted that the liquidation of a company raised a special equity because if the guarantor was not permitted to raise the set off he would be limited to proving in the winding up of the principal debtor and only receiving a dividend. Stirling J said: "It seems to me, therefore, that it would be inconsistent with the equitable right of a surety, and I think, therefore, that the set-off should be available to this extent." Isaacs J went on to say: "This and similar cases which deal with the state of affairs where a debtor is insolvent, are of no value or assistance, excepting perhaps to demonstrate that such cases are exceptions to the general rule that a guarantor cannot avail himself of the remedies which otherwise may be open to the principal debtor as against the creditor."

[25] Where the principal debtor is in liquidation there is some authority to support the proposition that the guarantor should be able to raise a defence by way of cross-action in circumstances such as exist here: *Langford Concrete Pty Ltd v Finlay* [1978] 1 NSWLR 14. There the New South Wales Court of Appeal was influenced by the fact that the guarantee in question obliged the guarantor "to pay what was payable, that is, payable by the debtor. It was not a guarantee to pay the price, or the price without deduction, but to pay only what the debtor could have been compelled to pay." (17) Then at 19 the Court said:

> "The principle that the guarantor should not be allowed to raise a defence by way of cross-action, unless the debtor is a party, is one for the benefit of the creditor; and this principle can be of no practical benefit to him where the debtor is in liquidation or insolvent. If he wishes to have the debtor bound, he is equally able to have it joined in the proceedings. Despite the theoretical difficulties involved, it seems to us that the guarantor should be allowed to raise this defence, and that the appeal should be allowed."

[26] After referring to that decision O'Donovan and Phillips go on to say at 550-1: "The procedure suggested in the case of a solvent principal debtor should also be adopted in the context of insolvency, that is, the principal debtor should be joined before there is a final determination of the issues between the parties." They reach that conclusion primarily because if the insolvent principal debtor was not joined as a party there was a "risk of subsequent action being taken against the creditor" by the liquidator of the principal debtor.

[27] As those authorities were not referred to in argument either before the trial judge or on the hearing of the appeal it is inappropriate for this court to express a concluded view on the question whether, in the absence of the insolvent principal debtor (Softex) as a party, the guarantor (appellant) could raise the counter-claim and set off pleaded in his defence. Suffice it to say that, speaking for myself, I have grave doubts that the appellant was entitled to litigate the issue in the circumstances which exist.

[28] Against that background I proceed to consider the merits of the appeal as it was argued.

[29] It was accepted by counsel for the appellant that the onus was on the appellant of establishing that the roller failed in circumstances establishing breach of warranty on the part of the respondent. Unless that was established the defence failed. In order to establish breach of warranty the appellant had to establish that the cause of the roller failing was de-bonding of the rubber covering applied by the respondent.

[30] The appellant presented scant evidence in support of its allegations. It did not have an independent expert examine at any time the roller in an endeavour to establish the cause of the failure. It did not take any photographs of the roller in its damaged condition and that meant that neither the court nor witnesses at the trial had the benefit of seeing the damage. More significantly the appellant's key witness Morris, the maintenance superintendent for Softex, did not make any detailed inspection of the damaged roller. He had no notes to assist him when giving evidence. Ultimately both at trial and on appeal the appellant's case heavily depended upon the evidence of Morris that the machine was working well and producing good quality paper up to the time of final failure.

[31] Against that, the critical witness for the respondent, Faoro, was able to give detailed evidence of his inspection of the roller a few days after it was taken out of the production line. Faoro, a qualified mechanical engineer, had been with the respondent (or its associated companies) for over 30 years and had extensive experience with rubber roll coverings. He gave evidence that he was "directly involved in looking at any quality concerns or product failures". When he inspected the failed roller he made notes and drew a diagram of one particular fault he observed. He was able to say that the rubber cover "had failed 12 inches in from the front side". At that point there was "separation and rubber had actually come away from the roll." But he was also able to say "there was still bonding solution and the metal itself was not visible during that inspection." It is clear from his evidence that the failure had been in a localised area and he expressed the view that it "could be mechanical damage in the form of a wrap". He described what he saw "as a mechanical failure, not a de-bonding". His evidence was that if there was de-bonding it would be seen over the whole roll. He also "observed that the surface of the rubber appeared charred"; that indicated to him there had been a "tremendous amount of heat build-up that caused that rubber to break down".

[32] He was extensively cross-examined and to some extent from time to time he modified under cross-examination what he had said in examination-in-chief. But his evidence was consistent throughout that the cause of the roller's destruction was not de-bonding of the rubber coating which had been applied by the respondent.

[33] Apart from Morris, the appellant relied on some evidence from the witness Meadows. After Softex went into administration the business, or some of the equipment, was put on the market. That resulted in Meadows visiting the Softex plant on about 5 October 2001 for the purpose of "doing due diligence" on behalf of his then employer. His evidence was that he "briefly" had a look at the subject roller which was still on the premises. He said: "I just briefly looked at it and so I didn't examine it in any detail." He then went on to say it "looked like a bond failure".

[34] The learned trial judge in his reasons said that Faoro "was the only witness to give worthwhile evidence of the condition of the roll in question following its failure." He noted that Meadows "saw the roll only briefly and on his own evidence did not examine it in any detail." He also noted that Meadows "had no worthwhile recollection". With respect to Morris the learned trial judge said: "Mr Morris seems to have had a very vague recollection of the inspection and of what had been pointed out by Mr Faoro. He also does not appear to have made a worthwhile examination of the roll himself." The learned trial judge set out at some length passages from the evidence of Faoro with respect to his observations and opinions. He then went on to say:

> "The observations of Mr Faoro, which I accept, are powerful indications that prior to the roll failing there had been serious overloading of the machine, excessive heat generation either secondary to or in association with chemical attack and some level of impact damage. The evidence of Mr Morris was that the machine was performing well and producing good quality paper up to the time of failure. I have difficulty in placing reliance on this evidence because it seems to be at odds with the serious damage that Mr Faoro noted.

> ...
>
> The principal argument advanced on behalf of the defendant really amounts to nothing more than the general proposition that a roll cover should not fail after a mere 23 days of operation. ...
>
> It simply cannot be concluded in these circumstances that the roll cover failed because of a defect in its manufacture. Mr Faoro's examination suggested that the roll had not debonded from the underlying metal. His inspection of the roll also suggested several signs of mistreatment of the roll cover which were of the type calculated to cause failure."

[35] In essence the learned trial judge found that the appellant had not established, the onus being on him, breach of warranty on the part of the respondent with respect to the provision of the recovered roller. That was a conclusion clearly open on the evidence. Given the paucity of detailed evidence from the appellant as to the condition of the roller that conclusion was hardly surprising.

[36] Ultimately before this court counsel for the appellant was driven to fall back on the proposition that the evidence established that paper production was good up until the time of final failure. It was submitted that the court should draw the inference from that that the cause of the problem was de-bonding and not mechanical failure or any of the other possible causes suggested by Faoro. I am not persuaded that the learned trial judge was wrong in evaluating the evidence as he did and in not drawing that inference.

[37] It follows that the appeal must be dismissed. Pursuant to the terms of the guarantee the respondent is entitled to indemnity costs.

[38] In the circumstances the appeal should be dismissed with costs to be assessed on an indemnity basis.

[39] **CHESTERMAN J:** It is a matter for regret that the parties did not argue the interesting question of whether, because Softex Industries Pty Ltd, the principal debtor, was insolvent the appellant guarantor could raise by way of defence to the action against him on the guarantee a claim for damages for breach of warranty which the principal debtor could have advanced if it had been sued for the debt. It is not, I think, obvious that the insolvency of Softex Industries Pty Ltd should alter the general principle identified in *Cellulose Products Pty Ltd v Truda* (1970) 92 WN (NSW) 561 that a guarantor cannot raise such a defence. The point was not, however, argued and I agree with Williams JA that we should express no opinion on it. I agree that the appeal should be dismissed for the reasons given by his Honour.