Puzzling Arithmetic

Rachel Barnes, April 2009

The causes of loss and damage are often complex and it is frequently alleged that more than one party is liable for the loss suffered. As a result, it is common for more than one party to contribute to a pay out.

For example, if a client makes a claim against a contractor because of defective work, the contractor can seek a contribution from the client's consultant on the basis that the consultant inspected the works and negligently failed to spot the defective parts, or where one consultant has produced a negligent design for a client and another who checked that design negligently failed to pick up the error.

If party A reaches a settlement with the claimant, it can still seek a contribution from party B towards the settlement sum. In practice, this can be complicated and have surprising results.

Suppose party A pays the claimant a settlement sum of £5m and thinks a 50:50 split between it and party B is fair. Party A might think it is entitled to recover £2.5m from party B. However, it does not work quite like that – not according to a recent court judgment, anyway.

According to this judgment, the division should be applied to the damage for which party A and party B are liable to the claimant for. Therefore, the amount of damage has to be assessed. Party A's proportion should then be deducted from the sum it has paid in settlement, and the balance is what party B should contribute. Suppose, the damage is assessed at £8m and the correct apportionment is 50:50: Party A would be entitled to recover only £1m from party B. This is the amount of the settlement sum (£5m) less half the damage (£4m).

The higher the assessment of the damage, the less party A will recover from party B. If the damage is £10m or more, party A would recover nothing from party B, even though party B was 50% to blame. Party A would be entitled to feel that Party B had benefited unfairly from the settlement terms it has negotiated with the claimant.

The complications may not end there. Party A and party B may both be liable for the same damage, but not necessarily for the same reason. For example, party A's liability to the claimant may be based on negligence, whereas party B may be liable only for breach of contract. Party A would have a right to claim contributory negligence against the claimant (assuming that there were grounds for making such a claim), which would reduce the amount the claimant could recover from party A.

Party B would have no such right, as contributory negligence does not apply to claims for breach of contract. How would this affect party A's claim for contribution against party B where party A has settled the claim from the claimant? Party A would want the reduction for contributory negligence to be applied to the overall assessment of the damage for which both are liable so the amount it can recover from party B is not reduced, even though only party A is entitled to a reduction for contributory negligence.

On this basis, and if the claimant's contributory negligence is assessed at, say, 25%, the damage is reduced from £8m to £6m. The apportionment between the parties is then £3m each and party A would recover £2m from party B as contribution towards the £5m that party A has paid in settlement. Party A would therefore get some benefit from its right to claim contributory negligence.

The court held, in the case referred to, that this was the right approach. However, the merits were rather clearer in that case, where the party in the position of party B had been held liable for deceit.

What would have been the position if there had been a contractual cap on party A's liability to the claimant? Say party A's liability had been limited in its contract with the claimant to the amount of the settlement sum, that is, £5m: party A would no doubt argue that the damage should be assessed as £5m on the basis that this was the most for which both parties could be liable to the claimant. Then, party A would then be able to recover 50% of the settlement sum from party B.

However, the court has held, in a similar situation, that a cap on liability does not affect the assessment of the damage. Therefore, the cap on party A's liability would not increase (or otherwise affect) the amount of contribution that it can recover from party B – a result that would no doubt surprise party A.

The effect of these cases will need to be taken into account when settling claims while a claim for contribution is still outstanding.

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