IN THE COURT OF APPEAL OF NEW ZEALAND

CA168/02

BETWEEN	EDGAR ALEXANDER Appellant
AND	GRAHAM CORNELL Second Appellant
AND	BETTALIFE INTERNATIONAL (NZ) LIMITED Third Appellant
AND	COFIE HOLDINGS PTY LIMITED Fourth Appellant
AND	GRAEME CLEGG First Respondent
AND	NEW IMAGE INTERNATIONAL LIMITED Second Respondent

Hearing: 26 & 27 May 2003

Coram: Keith J
Anderson J
Glazebrook J

Appearances: J G Miles QC and Z G Kennedy for Appellants
A H Waalkens and J Anderson for Respondents

Judgment: 25 March 2004

JUDGMENT OF THE COURT DELIVERED BY ANDERSON J

Nature and circumstances of the appeal

[1] This appeal and cross appeal against a judgment of the High Court (Salmon J) represent another round in a dispute between competitors in the business of

network marketing. Such business involves the distribution of goods through a network of individuals, any of whom may have a subsidiary network, resulting in a complex schematic of distribution traceable from a primary distributor who shares in the profits of sales made by subsidiaries, as do the subordinate heads of networks.

[2] The background and development of the dispute are discussed in a prior decision of this Court, *New World Property Ltd v New Image International Ltd & Anor* CA151/01 26 March 2002, and may be put briefly, at this stage.

[3] Mr Clegg, the first respondent, founded the second respondent in 1984. He remained the sole shareholder. The company manufactures health and so-called "lifestyle" products and distributes by networks. It operates in New Zealand and is the parent company of subsidiaries doing similar business in Australia and some Asian countries. One of the latter, until the end of 1999, was Hong Kong.

[4] Mr Alexander, who had been involved as a distributor with the Australian company from its inception in 1983, was recruited by Mr Clegg for the New Zealand company in 1988. He became the Chief Executive Officer of the Australian company in 1990 and returned to New Zealand in 1993 as International Vice President. In 1995 he resumed as Chief Executive Officer in the Australian company and so he remained until resigning in September 1998. He left the employment of New Image the following month, saying that he intended to pursue a business venture in the automotive industry.

[5] Mr Cornell joined New Image in Australia as a distributor in 1993. In April 1995 he entered into a joint venture agreement with New Image, involving the purchase by his nominee company of 26% of New Image's Hong Kong subsidiary. He became Managing Director of New Image Hong Kong from 1 May 1995 and was appointed Principal Distributor for Hong Kong.

[6] The Hong Kong Company initially traded profitably but by May 1998 had become insolvent. Negotiations between Mr Clegg and Mr Cornell resulted in an agreement for the former to buy out the latter. Mr Cornell's executive position with the company ceased from 11 August 1998.

[7] Both Mr Alexander and Mr Cornell were engaged on terms which included trade restraints and provisions as to confidentiality. The restraints proscribed the recruitment or solicitation of New Image distributors during the currency of the relevant distribution agreement and for six months after its termination, by the distributor on his own behalf or for any other direct selling or network marketing company. The confidentiality provisions acknowledged and protected New Image's proprietary interest in its confidential information which specifically included distributor lists and marketing plans.

[8] In October 1998 Mr Cornell and Mr Alexander met in Auckland and in Sydney. The discussions involved a representative of a company which manufactured skin care and nutritional products. Mr Cornell incorporated a company, Bettalife Hong Kong, in December 1998. It began operations in April 1999. Sometime in 1998 Mr Alexander became involved in a proposal to set up Bettalife in Australia and New Zealand. This involved the purchase, on 19 October, of an Australian shelf company, the fourth appellant Cofie Holdings Pty Ltd and the incorporation in New Zealand, on 4 December 1998, of the third appellant.

[9] Between August and December 1998 Mr Clegg became increasingly disquieted by information conveyed to him about the activities of Mr Cornell and Mr Alexander. It was thought that Mr Cornell was approaching people to encourage them to become distributors in Hong Kong for a new company to be called Bettalife. Rumours abounded in Australia, and New Zealand, Hong Kong and Malaysia about this new company. Mr Clegg was told that Mr Cornell was using New Image staff to help him. On 30 September 1998 Mr Clegg wrote to Mr Cornell complaining about what he had heard and asserting that Mr Cornell's conduct was in breach of the August agreement. Mr Cornell did not reply to that letter. In an earlier appeal this Court held that there was no evidence of solicitation by Mr Cornell of staff or distributors in Hong Kong. As to Mr Alexander, Salmon J found that he had encouraged four New Image distributors to join Bettalife, knowing that they were such distributors and that he was still bound by the restriction in his distributorship agreement and that it was unethical for him to do so. Particular distributors were Ms Conlay, Mr Gaffney, Mr Crawford and Mr Chuo.

[10] Mr Gaffney, who lived in Melbourne, had been a distributor for New Image since January 1993. Mr Alexander had recruited him as a distributor. Mr Gaffney testified that Mr Alexander contacted him in October and November 1998 and told him of a new company that he had started. According to Mr Gaffney, Mr Alexander told him that a ground floor opportunity was available if he wanted it and that he would have a greater earning capacity than he had with New Image. He had said that a number of New Image people had joined Bettalife.

[11] Ms Conlay of Adelaide had been a New Image representative since 1989. In October 1998 she received a letter advising of Mr Alexander's resignation from New Image and about a week later had a telephone call from Mr Alexander. He asked her whether she would like to join Bettalife and told her that all the key players in her Hong Kong network were joining him, and that New Image was in serious financial trouble. He said New Image owed him a considerable amount of money. She passed that information on to Mr Clegg. On 23 December she received a lengthy facsimile from Mr Alexander outlining the Bettalife marketing plan and encouraging her to join.

[12] Mr Crawford, of New Zealand, who had been a New Image distributor since November 1987, met Mr Alexander in Palmerston North in December 1998. Mr Alexander told Mr Crawford he was forming Bettalife and that he would like Mr Crawford and his wife to join. He said there were special privileges in joining early, that there were many New Image distributors joining and that he would have a thousand by early 1999. Mr Alexander said he considered that New Image would struggle to survive.

[13] Mr Chuo had been a distributor for New Image in Western Australia since July 1995. He learned that Mr Alexander had resigned from New Image and then, through Mr Richardson, a New Image distributor, he learned that Mr Alexander and Mr Cornell had formed a new company. This led to a discussion with Mr Alexander who told Mr Chuo that he should join Bettalife quickly because everyone was interested and Bettalife expected a thousand new members in New Zealand by the end of January.

[14] In December 1998 Mr Clegg had telephone discussions with Mrs Sue Kenyon, the administration manager of the Australian company. She told Mr Clegg about telephone calls from or about distributors who were being enticed to join Bettalife. Her information was that Mr Alexander and Mr Cornell were involved in that company and that there were comments and rumours being made about New Image being in a precarious financial position. Her evidence was that she had received telephone calls from distributors including Ms Conlay and these distributors had told her either that Mr Alexander or Mr Richardson had called and had said that New Image companies were in a bad financial position.

Pleadings and findings

[15] Mr Clegg responded to the information he was receiving by preparing a circular and sending it to his network of distributors. The appellants responded by bringing these proceedings for defamation and injurious falsehood. The principal defence is qualified privilege.

[16] Salmon J found that Mr Clegg was very upset by what was happening, that he considered Mr Alexander and Mr Cornell were behaving in an underhand way in setting up the competing company without any advice to him. Salmon J found that Mr Clegg considered the competing company and the activities of Mr Alexander and Mr Cornell were a serious threat to his company. It was because of this he decided to advise the distributors in New Zealand and Australia of what was happening. A circular was sent to 1,041 distributors in New Zealand and 473 in Australia.

[17] The amended statement of claim alleged, by reference to a number of paragraphs in the circular, that it meant the personal appellants were deceitful, unethical predators, financially untrustworthy, of no financial standing, lacking business skills and criminals. As to the corporate appellants, the pleading alleged that the circular meant the companies were engaged in unethical and dishonest practices, were financially unsound, were likely to fail, were such that no competent or honest person would work or be associated with them and were engaged in criminal activity.

[18] Salmon J found that there were words capable of meaning and which did mean that Mr Alexander was engaged in unethical practices, that Mr Alexander and Mr Cornell were likely to fail in their business activities and that they lacked business skills, and that the companies were financially unsound and likely to fail, both because of under capitalisation and because of a lack of business acumen on the part of Mr Alexander and Mr Cornell. He also found there were words which meant that Mr Cornell was acting unethically and that he lacked business skills, that both men were acting unscrupulously and were lacking in integrity, that they were unethical predators using proprietary information to steal vulnerable people from the network. The Judge also found that imputations against the owners and directors of the corporate appellants must necessarily reflect adversely upon the companies themselves and accordingly the same defamatory meanings as applied to Mr Alexander and Mr Cornell applied also to the corporate appellants. But he considered that references to "deceitful" added nothing to the imputation of unethical practices and that a reference to poaching other people's members being a crime did not carry a literal meaning of criminality.

[19] In relation to injurious falsehood, Salmon J found that certain statements made by Mr Clegg in his circular were false. These were to the effect that both Mr Alexander and Mr Cornell were using name lists and confidential information. To the extent that the circular carried the meaning that Mr Alexander and Mr Cornell had acted unethically, the Judge found that these were not proved to be false statements and the reference to "poaching other people's members is a crime" would be understood by a reader as no more than an imputation of acting unethically. But those statements which were false and injurious were not proved to have been made with malice. The Judge's findings in this respect are summarised at para [155] of his judgment:

> Mr Clegg said that he believed the statements he made in the circular were true. He obviously believed on the basis of what he had heard, that there was a very serious threat to the company. He felt betrayed that two executives who had considered he had supported should set up a competing business without any notice to, or discussion with him. He said that with the lateral transfer programme being undertaken by Bettalife his company could have wiped out if six key leaders were induced to cross. I have no doubt that Mr Clegg genuinely concluded that there was a very serious threat to his business. In those circumstances I do not consider that the statement about the use of lists of names was made recklessly as to whether the statement

> was true or false, nor do I consider that his sole or dominant motive was to injure the plaintiffs or that publication was with an indirect or dishonest motive.

[20] As to the defamatory meanings he had found, the Judge held that except in relation to the imputation of lack of financial standing on the part of each appellant there was no liability on the respondents because the defamatory words were published on an occasion of qualified privilege. New Image had a duty, or at least a right, to protect its distributors and their networks. It had an interest or duty to communicate information relating to threats to distributors and their networks and in relation to attempts to discredit New Image. The distributors had a corresponding interest to receive such information. He held that the appellants were not able to rebut the qualified privilege on the grounds of ill-will because they had not filed the Notice of Intention to Rely on Ill-Will, required by s41 of the Defamation Act 1992. The Judge declined an application for leave to file out of time, made by the appellants after ten days of trial.

[21] The Judge's exclusion from the defence of qualified privilege of some of the defamatory material is explained in para [107] of the judgment in these terms:

> The question that arises in this case is whether any of the defamatory material was "wholly unconnected with, and irrelevant to, the duty or interest which gives rise to the privilege". The privilege arises from the duty or right to protect the business of distributors from poaching or soliciting and to address perceived derogatory statements concerning the second defendant. Much of the defamatory material is directed at the financial standing of all four plaintiffs. The only way in which this could be said to be relevant is as a warning to distributors not to join the plaintiffs and their companies, because by doing so they will ally themselves with an organisation which is likely to fail. In my view, that warning is unconnected with and irrelevant to the duty giving rise to the privilege.

[22] Salmon J rejected defences of truth and honest opinion in relation to the defamatory material unprotected by qualified privilege.

[23] In the matter of damages, the Judge awarded Mr Alexander a nominal sum of $1,000 because he had acted unethically in poaching distributors. Mr Cornell, on the other hand, was not shown to have solicited distributors and in his case damages of $25,000 were awarded. As far as the corporate appellants were concerned, their damages were limited to loss of profits attributable to the defamation and the Judge

concluded that in relation to the third appellant these should be assessed at $12,567 together with interest in the sum of $1,285. In respect of the fourth appellant damages were assessed at $7,000.

The circular

[24] Against that background it is now convenient to set out parts of the published material emphasised by the appellants.

(a) "**We must keep our industry clean**.

> We are deeply saddened and upset that recent unethical and unacceptable activities detrimental to the security of our members, networks and businesses have necessitated the actions we have been forced to embark upon.
>
> **There is no deeper hurt than betrayal.**
>
> Eddie Alexander is involved in the systematic recruitment of New Image members to join another company - Bettalife.
>
> For some time now we have been receiving numerous calls from distributors in Australia and New Zealand upset about approaches being made to them and their downlines to join a company called Bettalife.
>
> The main complaint is that the integrity of our system is being undermined by what appears to be a blatant attempt to discredit our company. There is ill-feeling that ex-employees of the company would use name lists and confidential information to contact networks. This activity is causing dissension amongst members and is obviously an attempt for quick personal gain with no regard for the consequences."

(b) "*Australia*

> An application to register Cofie Holdings Pty Ltd (subsequently trading as Bettalife) was made on 19 October 1998. As at the 23 October 1998 the share capital is five ordinary $5 shares held by: Kay Choong Chia, (3) Eddie Alexander (1) and Graham Cornell (1). The registered office is 4 Mildura Place, Eleebana, New South Wales, the home address of Eddie Alexander. Applications have been made to reserve a name change to Bettalife International (Aust) Pty Ltd.
>
> *New Zealand*
>
> Bettalife International (NZ) Ltd was incorporated on the 4/12/98 with 100 shares. The sole shareholder is Mr E R Alexander. The

Directors are Mr E A Alexander and Mr Richard Alexander, (Eddie's son). The address is 112 Selwyn Road, Howick, Auckland (Mr Richard Alexander's home address)."

"An embarrassing statistic of the networking industry is the fact that 80% of companies fail in the first two years. The reasons for this are:

undercapitalised

inexperienced

lack of business acumen

ordinary products

money game/pyramid type marketing plans.

One of the main weaknesses is trying to run and develop a business from cash flow (Distributors' money) or inducing large sums of money from distributors in return for granting special status positions.

The network business is individually very personal and when companies crash the consequences are disastrous for those that TRUSTED THEIR LEADERS:

1. shattered dreams
2. loss of trust, disbelief and betrayal
3. absolute loss of all time committed
4. loss of future income and belief in the industry.

New Image has been in business for 15 years and over that period of time, from our own manufacturing plant we have developed a number of truly exceptional, market leading products. It would be unusual to think that a new company could accidentally come into possession of an exceptional product that could become a market leader. Statistically, the odds just do not stack up. It would be fair to say, the bigger the promises, the bigger the inducements and the harder the talk, the more suspicious one should be. Use Due Diligence when checking a company out."

(c) "*Hong Kong*

We are very proud of the day that Graham Cornell became a joint venture partner in Hong Kong. When following company policy, the Hong Kong company was very profitable and the prosperity was shared with many distributors making high incomes. Unfortunately, there was a shift in product emphasis and the core business over the last 18 months. A serious deterioration in sales took place, culminating in a decision to restructure the joint

venture. This was announced in our birthday edition newsletter of October. The new joint venture is proceeding successfully with brand new offices in Kowloon. Obviously, the joint venture settlement with Graham Cornell contains many confidential aspects, but the audited accounts verify a very good profit in the 1995/96 year and unacceptable losses in 1996/97 and 1997/98 necessitating the restructuring.

Graham Cornell introduced a company called C-Tech to partner him but they declined to support his proposal when we met in Hong Kong. Only then did we enter into negotiations with Totalife Taiwan.

Mr Alan Stewart, Chartered Accountant from New Zealand assisted with the documentation for the Cornell settlement. The following clause becomes quite relevant under the circumstances.

"Cornell to use his best endeavours to protect the goodwill of NZ New Image Hong Kong Limited and New Image International, including assisting with the handover to new management, maintaining good relationships with staff and distributors and not in any way upset the good relationship of all parties."

On the 11th August New Image paid a very substantial US dollar part payment to Graham Cornell to activate the agreement. It deeply saddened me that within days of signing this agreement, I was informed from a number of sources that Graham Cornell was talking with people in Hong Kong about forming Bettalife and trying to attract people and financial capital. I must confess, this behaviour was totally unexpected and unacceptable.

As Graham Cornell is totally implicated in the Bettalife company and strategy, I feel responsible to make it publicly known that his 26% shareholding investment in Hong Kong was all borrowed money."

(d) "It will be obvious from the above information that New Image International is totally committed on a long term basis to the Australian company and see it as a very important member of our Group. The magnitude of our financial support will be a surprise to many members. It must give great confidence to everyone to know their New Image cheques will always be honoured and their efforts rewarded because of our commitment. It is our intention to make Australia the flagship of our company."

(e) "Names of key New Image people are being touted as converts to Bettalife. Murray Crawford, Sau Yip, John Tay and Patrick and Helen Chong are angry that their names have been unscrupulously used. Murray Crawford is on circuit in Australia in March conducting New Image meetings and reinforcing that our product range is unsurpassed in the industry. Name dropping is a common tactic mostly used by unscrupulous people."

(f) "It is regretful that Eddie appears to be similarly implicated in the same tactics that he took some distributors to task about in West Australia a couple of years ago. He therefore knows exactly the values, morals and ethics related to this behaviour.

He also knows the consequences. New Image did not instigate this unfortunate matter or in any way put stories in the market place. The perpetrators chose to conduct a systematic campaign to solicit our people and make the statements answered in this communication. This forced our official response and if our members become aware of additional statements detrimental to and unfair about our company, they should be reported immediately. The management assures all members of our total support to protect the integrity of the system - to protect your networks - to protect your livelihood and income from exploitation and unfair attacks."

(g) **"There is no right way to do a wrong thing. Ethics and integrity will not be compromised.**

New Image is committed to the protection of the sponsorship principles which professional and respectable companies in the Direct Sales Industry consider are sacrosanct. Most members are unable to defend themselves from unethical predators who use their positions and proprietary information to steal vulnerable people from their network. In normal business, actions like shoplifting, insider trading, breach of trust, proselytizing and use of proprietary information for personal pecuniary advantage is dealt with severely by the courts. Poaching other people's members is a crime."

(h) "Tactics of this nature are used by greedy people everywhere and, when they are unable to succeed in creating a large Direct Sales Team themselves, they succumb to the temptation of trying to get to the top on the backs of others. This only leads to resentment with people being hurt."

(i) "All members should be aware that there is a temptation for unscrupulous people to try to reverse the hierarchy through unethical practices instead of hard work. The law of the universe says: Persist and get it right and ownership will be yours.

The Direct Sales Industry is brought into disrepute when vulnerable people are enticed by unrealistic promises and inducements which are offered with the express purpose of benefiting the perpetrator.

Eventually people will realise they were used, but the unfortunate result is many casualties. Most people know right from wrong and avoid temptation. Obviously these tactics are morally wrong and distributors themselves should take a firm stand and stamp the practice out."

(j) "As a distributor you are the "guardian of the dream". If you witness illegal and unethical practices you have a responsibility to all members to report matters to the company. Let's keep our whole industry clean and respectful."

Procedural issues

[25] The respondents put in issue on this appeal, as well as the substantive matters already mentioned, two procedural rulings by Salmon J. The first is a ruling declining the respondents' application in the course of trial for an order requiring production of the financial accounts and budgets of Bettalife International (HK) Ltd. The second was a ruling, also in the course of trial, that this Court's judgment in the earlier proceeding raised an issue estoppel against the respondents from contending that Mr Cornell's solicited distributors of New Image (Hong Kong) to persuade them to join his company, Bettalife (HK). Nor could the respondents traverse matters relating to the share sale agreement which had been determined, also, in the previous appeal.

Appellants' submissions on appeal

Defamation

[26] Counsel for the appellants submitted that Salmon J erred in holding that the words of the circular were not capable or did not mean that the appellants were "financially untrustworthy" and "guilty of criminal conduct". Also, the Judge erred in conflating "unethical" conduct with "deceitful" and "unscrupulous" conduct. It was contended that those words have significantly more serious connotations and the Judge's findings were all directly material to the issue of damages.

Injurious Falsehood

[27] Counsel submitted that the Judge erred in holding that Mr Clegg had not acted with malice as the false statements found to be made could not have been made without the necessary element of recklessness. Mr Clegg had no evidence that the appellants were using New Image name lists. In respect of the attack on the financial

stability of the companies, Mr Clegg must have known that it was commonplace for companies to be registered with a notional capital structure that would be altered when the company began operations. Mr Clegg failed to check any of his assumptions. Moreover, there was clear evidence that the real reason Mr Clegg was so aggressive was that he believed that the appellants were not entitled to set up a competing company.

Damages

[28] The appellants accept that an appellate court will normally not interfere with an award of damages by a Judge unless satisfied that the Judge has acted upon a wrong principle of law, has misapprehended the facts or has taken into account irrelevant factors (*Davies v Powell Duffryn Associated Collieries* [1945] 1 All ER 657). However, they submitted, the Judge erred in assessing the damages awarded to Messrs Alexander and Mr Cornell for two reasons.

[29] First, the Judge was wrong to limit damages because of "unethical conduct" on the part of Messrs Alexander and Cornell. The "unethical conduct" of Mr Alexander could not justify the character assassination perpetrated on him. Moreover, the finding of "unethical conduct" against Mr Cornell based on Bettalife's offers of what was known as "lateral transfer", i.e. recruitment to an analogous position in the recruiting network, cannot stand as the practice was barred only by the World Association's Code of Practice and not by the New Zealand Code (at that stage).

[30] More importantly, counsel for the appellants submitted that the main sting of the defamation was the charge of lack of business acumen and financial credibility. This was particularly damaging to the appellants, given the importance placed on these factors in the network marketing industry and the vulnerability of their start-up company to these allegations. These allegations were made in direct contradiction of the facts as known to Mr Clegg and were grossly reckless.

[31] In respect of the damages awarded to the company, the appellants submitted that damages should include compensation for all losses that were "reasonably

foreseeable as a result of the defamatory statements contained in the circular". Counsel made two specific submissions. First, that the Judge erred in preferring the evidence of the respondents' expert to that of the appellants' in relation to the New Zealand company. The appellants' evidence was clearly preferable as it used actual sales figures to more accurately project the loss of profits that would have been generated in the six-month period. The respondents' evidence represented an entirely artificial assessment that ignored the fact that the company was not operating in a mature market but rather in a growth phase. Secondly, that the Judge erred in failing to assess damages in relation to the Australian company on the basis of reasonable foreseeability. It was reasonably foreseeable that the company would develop along similar lines to the New Zealand company. It was foreseeable that the effect of the circular would be to mortally wound the companies. The lack of effort was reasonable (given the companies were operated essentially as joint ventures) and foreseeable. As such, no discount should be made for this.

Respondents' submissions on appeal

Defamation claim

[32] The respondents' supported the Judge's findings as to the meaning of "crime" in competition with poaching, asserting there was clear evidence that the network marketing industry considered "poaching" not only as unethical but also as "stealing" and "theft" and that under the "laws" of the industry, poaching was considered a crime. The Judge's finding that the circular did not carry the meaning that the appellants were financially untrustworthy was open to him. Alternatively, the respondents submitted, the additional meanings fall within qualified privilege or in any case did not add to the damages.

Injurious falsehood

[33] The respondents submitted that the appellants have attempted to apply an incorrect test. "Recklessness" in a defamation context is treated as knowledge of falsity and is not to be equated with carelessness, impulsiveness or irrationality: *Gatley* para 32.34. Here there was no evidence that Mr Clegg was indifferent as to

the truth of the appellants' use of name lists or guilty of any improper motive: Mr Clegg was not cross-examined on these matters.

Damages

[34] The respondents submitted that the Judge was fully entitled to accept their expert's evidence. His approach was entirely conventional and acceptable. In any case, there was evidence that profits were not expected to be high, that growth would be slow for at least the first 3 months of a new network marketing business. As such, the drop-off in sales cannot be attributed solely to the non-privileged parts of the circular.

Respondents' submissions on cross-appeal

Defamation – Qualified privilege of financial statements:

[35] The respondents submitted the Judge erred in considering whether the financial statements fell outside the occasion of privilege, given the Judge's findings on s41. The respondents submitted that issues going to irrelevancy of material published on occasions of privilege are dealt with under s19 of the Defamation Act in deciding whether the defendant has: "otherwise taken improper advantage of the occasion of publication". The inclusion of separable material does not render an occasion no longer privileged: *Dunford Publicity Studios Ltd v News Media Ownership* [1971] NZLR 961, 968; *Horrocks v Lowe* [1975] AC 135, 151. Therefore, by failing to file the appropriate s41 notice, the appellants could not argue that some material in the circular fell outside the privileged occasion.

[36] Alternatively, counsel for the respondent submitted the Judge had erred in holding that the financial statements were outside the privileged occasion. The respondent makes five independent points.

[37] In *Horrocks v Lowe*, Lord Diplock made statements to the effect that irrelevant defamatory matter incorporated into a statement made on a privileged occasion will not be actionable outside the privilege, but will rather go to show

malice. *Horrocks v Lowe* has been followed by this Court in *Reeves v Saxon* CA134/89, 17 December 1992.

[38] In any case, the financial information was relevant to the subject with respect to which the privilege exists as defined by the Judge – the topic of distributors potentially defecting. Information to assist a distributor in making a decision to defect would be relevant to that subject.

[39] The financial statements should be protected as a response to the appellants' attack on New Image as defined by the Judge. The respondents submitted that a wide latitude is given to respond to defamatory attacks: *Watts v Times Newspapers* [1996] 2 WLR 427, *Adam v Ward* [1917] AC 309, *Penton v Calwell* (1945) 70 CLR 219.

[40] The Judge erred in defining the privileged occasion. Because of the loyalty inherent in a network marketing chain, there is a duty and interest to warn distributors of the risk of moving allegiance to an organisation that may fail due to financial/business reasons. An analogy is drawn with trade association cases (communications about credit) and employers' references.

[41] It was submitted the Judge had erred in holding that the statements about financial information could be severed from the statements about integrity. In many cases, the same phrases in the circular were used to support both meanings.

Damages

[42] The respondents further submitted that the Judge had erred in assessing the damages awarded to Mr Cornell by awarding more than nominal damages. In the earlier proceeding, this Court found that Mr Cornell, although not soliciting New Image clients, had engaged in conduct that was unethical. Moreover, Mr Cornell was closely associated with the Australian business and its poaching activity.

[43] Counsel submitted that the judge also erred in determining damages in respect of the companies by failing to base damages only on that part of the circular dealing with financial statements, as opposed to the whole circular. The respondents' expert's evidence, which the Judge accepted, measured the loss of profits caused by the whole circular. Given that the majority of the circular concerned ethics and not financial matters, only a portion of the experts' assessment should have been awarded.

Production of accounts

[44] Counsel for the respondents submitted the Judge had erred in holding that the financial accounts of Bettalife Hong Kong were not relevant and that it was too late to require production. The accounts of the company from start up would provide a yardstick by which the performance of the New Zealand and Australian companies could be measured. This in turn would enable a better assessment of whether the stagnation was due to the circular or to general market conditions. To refuse to discover them on the basis of inconvenience was to condone the failure of the appellants to discover the documents.

Issue estoppel

[45] Counsel for the respondents submitted that the Judge had erred in finding an issue estoppel against the respondents because the appellants did not plead that. Alternatively, counsel submitted, the issues were not identical. The issue in the earlier proceedings was whether Mr Cornell's activities breached a contractual clause requiring his best endeavours to protect goodwill. The wider issue in the present case was whether there was unethical or unacceptable action by Mr Cornell.

Appellants' submissions on cross-appeal

Defamation – Qualified privilege of financial statements:

[46] The appellants submitted that the respondents' reliance on *Horrocks v Lowe* was misplaced. They submitted that the dictum of Lord Diplock is inconsistent with

established authority (in particular *Adam v Ward*), has been questioned in *Gatley* (para 14.9) and has not been followed in the United Kingdom or Australia: *Watts v Times Newspapers; Bellino v Australian Broadcasting Corporation* (1996) 185 CLR 183. Neither qualified privilege nor allegations made in response to an attack will protect defamatory statements irrelevant to the privilege or to responding to the attack. There is a clear distinction between the ambit of the privilege and the rebuttal of the privilege due to malice.

[47] The appellants further submitted that a privilege on this occasion could arise only from the duty to protect the business of distributors from poaching and to respond to defamatory comments from the appellants. There was no duty to "warn" distributors about the dangers of joining another network. And the financial statements did not respond to the allegations made against New Image. Finally, the appellants submitted, the statements regarding financial information were not so inextricably linked with statements on ethical matters in the circular as not to be severable. The two issues were clearly independent.

Damages

[48] The appellants submitted that this Court's earlier finding of no solicitation disposes of the first matter. As to the second matter, the appellants submitted that the Judge clearly directed himself to the need to distinguish between those comments in the circular which were subject to qualified privilege and those which were not. The appellants submitted that the Judge considered, and properly so, that the loss sustained by the companies was attributable to the financial statements. In any case, a defendant will be liable for any loss suffered where the defendants' tortious breach of a duty was a material cause of the damage: *Schilling v Kidd Garrett* [1977] 1 NZLR 243.

Production

[49] The appellants submitted that the Judge took the appropriate course. The probative value of the evidence was questionable, there being no evidence as to the difference in market conditions between Hong Kong and New Zealand. There was

no prejudice as it should have been clear to the respondents well before trial that the appellants did not consider the material relevant, yet no issue was taken with this stance.

Issue estoppel

[50] The appellants acknowledge that the issue was not pleaded in the statement of defence but submitted that at the time this was drafted it was not clear what evidence the respondents would call. The respondents did not seek an adjournment at the time and even now do not assert that they suffered prejudice. The appellants also submitted that the Judge clearly limited the estoppel to the issue of solicitation and was clear that it was still open for the respondents to call evidence to establish unethical behaviour. The respondents cannot now use their default to justify an appeal.

Discussion

[51] The linchpin of the appeal as to defamation and the cross appeal in its entirety is the correctness or error of the Judge's determination on the issue of qualified privilege. It is therefore convenient to deal with that issue at the outset of this discussion.

[52] Salmon J found that except in one respect the alleged defamatory words were published on an occasion of qualified privilege and were protected by that. This was because New Image had a duty, or at least a right, to protect its distributors and networks; because New Image had an interest or duty to communicate information relating to threats to distributors and their networks and in relation to attempts to discredit New Image; and the distributors had a corresponding interest to receive such information. But some of the words spoken of the appellants amounted to a warning to distributors not to join the appellants because, allegedly, the distributors would be in an organisation which was likely to fail. The Judge held that such a warning was unconnected with and irrelevant to the duty giving rise to the privilege.

[53] In our view the Judge erred in so holding.

[54] It is not necessary for us to attempt to resolve the conflicting views that, on the one hand, the relevant defamatory matter incorporated into a statement made on a privileged occasion will not be actionable outside the privilege but may be relevant to malice, and on the other hand that such irrelevancy removes the defamatory words beyond the pale of the privileged occasion and leaves them unprotected by it. Were the former view to be preferred, the appellants could not take up the issue of malice because of their omission to file a notice pursuant to s41 of the Defamation Act 1992. But if the latter view were to be preferred the words complained of were, in our view, sufficiently relevant to and connected with the circumstances giving rise to the privileged occasion.

[55] Our reasons for so holding begin with the elucidation of the nature of qualified privilege expressed in the *Laws of New Zealand*, *Defamation* para 101, and adopted by Salmon J in the course of his judgment:

> In order for the publication of defamatory matter to be protected by qualified privilege, the communication must be made by a person having an interest or duty, whether legal, social or moral, to make it to the person to whom it is made; further the person to whom it is made must have a corresponding interest or duty to receive the communication. The privilege extends only to communications concerning the subject with respect to which privilege exists; it does not extend to anything that is not relevant and pertinent to the discharge of the duty the exercise of the right or the safeguarding of the interest which creates the privilege. Examples are statements made for the protection or furtherance of an interest to a person who has a common or corresponding interest to receive them, statements made in protection of a common interest, and statements made in answer to inquiries; alternatively, there must be an appropriate status and subject matter to confer the privilege, such as exists in the case of fair and accurate reports of judicial or parliamentary proceedings. Irrelevant matter is not privileged; however, it does not destroy the privilege attaching to the rest of the material.

[56] Salmon J was of the view that the privilege in the present case arises from the duty or right to protect the business of distributors from poaching or soliciting and to address perceived derogatory statements concerning New Image. Qualified privilege in those circumstances was considered by Dixon J in *Penton v Calwell* (1945) 70 CLR 219 at 233 in the following terms:

> When the privilege of the occasion arises from the making by the plaintiff of some public attack upon the reputation or conduct of the defendant or upon some interest which he is entitled to protect, the purpose of the privilege is to enable the defendant on his part freely to submit his answer, whether it be

> strictly defensive or be by way of counter-attack, to the public to whom the plaintiff has appealed or before whom the plaintiff has attacked the defendant. The privilege is given to him so that he may with impunity bring to the minds of those before whom the attack was made any bona fide answer or retort by way of vindication which appears fairly warranted by the occasion. … The foundation of the privilege is the necessity of allowing the party attacked free scope to place his case before the body whose judgment the attacking party has sought to affect.

[57] In the High Court of Australia, in the same case, Latham CJ and Williams J at 242-243 held:

> Statements which are made in self-defence are privileged when they are made in reply to attacks upon the character or conduct of the defendant, or in protection of an employer against attacks on the employer, or in protection of the proprietary interests of a defendant or his employer against attacks upon such interests.

[58] The terms of a defensive response are not judged to a nicety, as Lord Diplock acknowledged in the following terms in *Horrocks v Lowe* [1975] AC 135, 151:

> The exception is where what is published incorporates defamatory matter that is not really necessary to the fulfilment of the particular duty or the protection of the particular interest upon which the privilege is founded. Logically it might be said that such a relevant matter falls outside the privilege altogether. But if this were so it would involve the application by the Court of an objective test of relevance to every part of the defamatory matter published on the privileged occasion; whereas, as everyone knows, ordinary human beings vary in their ability to distinguish that which is logically relevant from that which is not and few, apart from lawyers, have had any training which qualifies them to do so. So the protection afforded by the privilege would be illusory if it were lost in respect of any defamatory matter which upon logical analysis could be shown to be irrelevant to the fulfilment of the duty or the protection of the right upon which the privilege was founded.

[59] Lord Diplock's approach was favoured by this Court in, for example, *Reeves v Saxon* CA134/89 17 December 1992. In any event, whether excessive retaliation to circumstances invoking qualified privilege should be rejected as falling outside the privilege or as constituting evidence of malice, the question of excess should not be examined narrowly and without keeping in mind the policy justification for recognising the privilege at all. We think, with respect, that Salmon J took too narrow a view having regard to the circumstances which gave rise to the privilege and the features of the attack which broadly indicate the scope of the permissible response.

[60] The context of the respondent's circular is the symbiosis of the network style of distribution. Every member of a primary or subsidiary network depended on the continuing, efficacious business activity of related modules. If one member or module should be removed from the network there would inevitably be financial harm to many. We do not doubt that in these circumstances those who shared a common interest in the functioning of the relevant networks had a duty to advise of perceived risks both to those who remained in the networks and those who shifted allegiance, and those who were so advised had a duty to receive the same. Salmon J held as much.

[61] But there is another facet of the jurisprudence of qualified privilege which is apt in this case. That is the privilege to hit back when one's reputation is attacked.

[62] Here, as well as those matters which rightly commended themselves to Salmon J as falling within an occasion of qualified privilege there is an attack made on the New Image operation in respect of its financial soundness. Mr Alexander was putting it about, as the Judge's findings confirm, that New Image was in serious financial trouble. Indeed, the financial vulnerability of New Image and the optimistic financial prospects of Bettalife were stressed by Mr Alexander in his soliciting of New Image's distributors. He was doing this for the benefit of all the appellants. It is the case that similar conduct was not demonstrated on the part of Mr Cornell, but in the volatile situation of the poaching and impending competition, such being believed to be unlawful and unethical, it would be unrealistic not to regard the position of all the appellants as synonymous for the purposes of the relevant privilege. There was such a close association between Mr Alexander as he put about the supposed financial instability of New Image, and the other appellants who were parties to the opposing venture, as to bring all within the scope of the privileged occasion. Absent ill-will, or malice as it was conventionally known, all the appellants were within the lawful range of the respondent's counterpunch.

[63] In short, Salmon J was wrong to find, in effect, that the respondents had to keep one hand behind their backs and were permitted to retaliate to only some of the appellants' blows.

[64] In our opinion the publication was, in its entirety, protected by qualified privilege and the respondents are entitled to succeed on the cross-appeal.

[65] We turn now to the Judge's other fundamental conclusion which was that the claim of injurious falsehood failed because the appellants had not proved malice. It will be recalled that Salmon J found that the publication carried the meaning that the appellants used lists of employees of the second respondent for confidential information relating to the second respondent in order to recruit employees. The Judge rejected other allegations. One was that the corporate appellants were inadequately capitalised to fund their respective businesses. Salmon J held that on the basis of the information available from the company's offices in Australia and New Zealand it would be reasonable to conclude that the companies were not adequately capitalised to conduct a business in which they were engaged. Nor was it established to the Judge's mind that Mr Clegg made such statements knowing they were false or reckless. The Judge also rejected an allegation that the circular conveyed the meaning that the appellant's products were not sourced from reputable suppliers and were not of the quality of those sold by the second respondent. In the Judge's view the circular did not carry such meaning. A further alleged meaning was that the appellants had acted criminally, deceitfully or unethically. The reference to criminality derives from the statement in the circular that "poaching other people's members is a crime". The Judge took the view that a reader would not understand the reference to the breach of the criminal law but rather that in the world of network marketing poaching was regarded very seriously. In other words, the Judge has effectively found that in its context and having regard to the confining of readership to members in the network, "crime" carried not its more technical meaning but rather connotations of moral turpitude. He held that in context the reference would not be taken as meaning anything more than that the appellants had acted unethically and Mr Alexander had in fact so acted. But the Judge found that Mr Cornell had also acted unethically in the sense that he sought to entice by lateral transfer which was conduct proscribed by the World Direct Selling Federation Code of Ethics.

[66] The Judge's findings in the matter of malice are set out in paragraphs [154]-[156] as follows:

> The question then is whether in respect of the claim that the plaintiffs used lists of employees, such statements were made maliciously. Mr Clegg's evidence did not specifically address the statement that the plaintiffs used lists of employees. He was aware that some of the documents prepared for Bettalife were almost identical in their wording to documents used by New Image. He had received reports that New Image members were being solicited. In reliance on the information that he received, particularly from Mrs Kenyon and Mrs Fettes, he drew the conclusion that Mr Alexander and Mr Cornell were attempting to start a business based on New Image contacts including its distributors. It seems he made the assumption that name lists were being used. On the evidence his assumption was incorrect. The question is, whether in the circumstances that was a reasonable assumption.
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> Mr Clegg said that he believed the statements he made in the circular were true. He obviously believed on the basis of what he had heard, that there was a very serious threat to the company. He felt betrayed that two executives who he considered he had supported should set up a competing business without any notice to, or discussion with him. He said that with the lateral transfer programme being undertaken by Bettalife his company could have been wiped out if six key leaders were induced to cross. I have no doubt that Mr Clegg genuinely concluded that there was a very serious threat to his business. In those circumstances I do not consider that the statement about the use of lists of names was made recklessly as to whether the statement was true or false, nor do I consider that his sole or dominant motive was to injure the plaintiffs or that publication was with an indirect or dishonest motive.
>
> Accordingly, I am not satisfied that the plaintiffs have discharged the onus upon them of establishing malice. The second cause of action, therefore, must fail.

[67] The Judge had the benefit of observing Mr Clegg, assessing his motives and honesty in light of the trial as a whole and has formed a view about his genuineness. We have not been persuaded to take a different view from him in the matter of Mr Clegg's honesty.

[68] It was submitted on behalf of the appellants that Mr Clegg must have been reckless because he had no evidence to support his allegations and took no steps to check their accuracy. But recklessness in the case of injurious falsehood as in many other jurisprudential concepts has the implication of not knowing whether a fact be true or false and not caring. A genuine belief that facts are true may reflect carelessness but not recklessness.

[69] On this fundamental aspect of the appeal the appellants fail.

[70] All the other issues raised on the appeal do not call for an answer having regard to our conclusions on the issues of qualified privilege and absence of malice in relation to injurious falsehood but for the sake of completeness we will briefly address them.

[71] On the matter of damages we would not have interfered with the Judge's assessment. The true sting of defamation lies in the impact on the injured party's reputation in consequence of how the words complained of would be understood by a reader. It may add to the weight of criticism but not to any meaningful appreciation of it to analyse, semantically, the different values of terms such as "unethical" "unreliable" "unscrupulous" "dishonest". The disparaging connotations are the real cause of injury. In this case the publication was to members of a defined group, namely the constituents of the New Image network. Reputational damage was therefore in the eyes of people who would know that the disparagement was for poaching by an allegedly unsound organisation which was bound to fail. On the Judge's approach only the disparagement of financial prospects was actionable. But the people to whom the defamation was published were not potential purchasers at retail but prospective distributors in the poaching network. Any economic loss in these circumstances must have been confined to the economic consequences of potential distributors being deterred from switching allegiance by the imputation of lack of a financial future. Damage to reputation in the financial sense had to be weighed against justifiable diminution in reputation arising from the unethical conduct. We see no basis for interfering with the Judge's assessment of damages in respect of the personal appellants nor any reason to contradict his preference of expert evidence in relation to the corporate appellants.

[72] Concerning the matter of production, we see no basis for disagreeing with the Judge's conclusion that further production should not be ordered at the stage the litigation had reached. Trials are not to be regarded as roving commissions where inquiries are made into every matter of interest or concern that arises en route. Discovery of documents with its attendant inconvenience and cost is recognised as one of the banes of modern litigation and ought be constrained rather than extended. In any event, the respondents are quite unable to point to any disadvantage, in pecuniary terms, flowing from the prohibition on production.

[73] On the matter of issue estoppel we agree with the submissions on behalf of the appellants, set out at para [50] of this judgment that the respondents can point to no particular prejudice.

[74] For the above reasons the appeal fails and the cross-appeal succeeds. Judgment should be entered in the High Court in favour of the respondents. The respondents are also entitled to costs in this Court in the sum of $12,000 together with usual disbursements as fixed by the Registrar.

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