

IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY

A. No. 293/82

730

BETWEEN EUNICK MANUFACTURING LIMITED

Plaintiff

A N D ALL PLASTICS LIMITED

Defendant

Hearing: 28, 29 & 30 May 1984

Counsel: R. Chapman for Plaintiff
M.P. Reed for Defendant

Judgment: 4/7/84

JUDGMENT OF QUILLIAM J

This is an action for damages arising out of a contract for the manufacture and supply of certain toys.

The plaintiff (Eunick) is a manufacturer and distributor of plastic toys of various kinds and of a wide range of other articles for the use of infants and young children. In 1979, in the course of this business, it imported from Greece some toys to which I refer as Roll-a-Duck balls. These comprised two clear plastic hemispheres glued together to form a sphere, inside which was a liquid on which floated a small plastic duck. The principle was that no matter what was done to the sphere the liquid inside it would find its own level and so the duck would constantly finish in an upright position. Eunick's import licence allowed it to obtain only a few of these toys but it was quickly appreciated that they were likely to have a strong market appeal. Those which were imported sold at once and Mr Curtis, the Managing Director and principal

shareholder of Eunick, was anxious to develop what he believed to be a potentially substantial and profitable market. He therefore decided to try and have toys of the same kind manufactured in New Zealand.

He went, first, to a firm of plastics manufacturers called N.Z. Electroformers Ltd (Electroformers) who were already doing a good deal of work for Eunick. He showed Electroformers one of the Greek Roll-a-Duck balls and invited them to make the same kind of thing. An agreement was concluded for Electroformers to make the necessary moulds and dies and to fulfil an order for 10,000 Roll-a-Duck balls. Some of these were duly made and for the plastic spheres a material known as K Resin was used. The liquid inside was water containing a small quantity of a fungicide known as Nipogen and the duck was made of a plastic similar to that used for the Greek ducks. One of the problems which had to be solved was a means of ensuring that the duck would float in an upright position and not roll on to its side or upside down. This had been achieved in the Greek ducks by placing in a compartment underneath the duck a metal washer which was of sufficient weight to keep the duck in the correct position. Electroformers used a similar principle but with some differences. In the Greek duck the washer was encased in a plastic sachet in order to prevent the water reaching it. Electroformers placed a galvanised washer in the compartment under the duck and on top of it put a material known as Dum Dum. This is a type of viscous sealant. There was a conflict as to whether the Dum Dum was inserted to protect the washer from water or to seal the hole left on the inside of the duck in the course of the manufacturing process, or perhaps both. I shall return to this later.

Mr Curtis's forecast as to the likely popularity of these toys was evidently well founded. Although the

arrangement with Electroformers was for the manufacture of 10,000 balls only about 3,000 were supplied. These sold so readily that Mr Curtis was anxious to obtain more as soon as he could, but Electroformers were not able to meet his requirements. A few problems were encountered with these balls but only to the extent of about 1% of those supplied. In some cases the sphere had not been adequately glued and water leaked out. More particularly, it was found that in some cases water had got inside the ducks which had upset their balance and meant that they tended to sink. For the most part, however, the articles supplied were satisfactory and the principal complaint by Mr Curtis was one of inadequacy of supply.

In order to try and get a more reliable supply and to get it quickly while the enthusiasm of the market for this rather novel product remained, Mr Curtis decided to look elsewhere. He approached the defendant (All Plastics) who had filled promptly an order he had given them for another product. Accordingly, in about June 1980, he went to see Mr Billing and Mr Collier, the two directors of All Plastics. There were several discussions in some of which Mr Curtis was accompanied by his General Manager, Mr Maguire. The matters discussed were whether All Plastics could manufacture the product and, if so, at what price. Basically Mr Curtis wanted the same product as had been made by Electroformers but with one main variation. This related to the problem of water getting inside the ducks. Mr Curtis showed All Plastics both the Greek product and also that made by Electroformers and these were taken apart and examined. Mr Billing and Mr Collier were not impressed by the use of the Dum Dum material and various alternatives were discussed. They suggested different materials for the washer and, in particular, proposed washers made of plastic or of stainless steel. Mr Curtis would not agree to these

suggestions and specified that the washers should be of galvanised steel.

It was the evidence of both Mr Billing and Mr Collier that they warned Mr Curtis it would be impossible to prevent water reaching the washer and that this was something which must be accepted. This was denied by Mr Curtis, who said that he stressed the washer should not come in contact with water or it would become rusty. This is the matter which is at the heart of the action and I shall return to it later.

Agreement was finally reached between the parties and on 17 September 1980 Mr Curtis completed a written order for the manufacture and supply of 18,000 Roll-a-Duck balls for delivery within five weeks, if possible. This order was written out on a printed order form normally used by Eunick and which had, on the reverse side, a number of conditions to which the order was expressed to be subject. The plastic spheres for this first order were made of K Resin. The ducks were redesigned by All Plastics to the extent that two variations were made from the type of duck made by Electroformers. The latter had eyes set on stalks which fitted into holes in the head. It was thought that this may have accounted for some of the water getting into the duck but, in any event, it involved an additional step in the manufacturing. It was agreed there should be no holes for the eyes but that they should be painted on. The second change concerned the cap holding the washer. As I have said, All Plastics considered the use of Dum Dum inefficient. They redesigned the cap by adding to it a plastic spike which, when the cap was in position on the duck, would fit tightly into the hole in the bottom of the duck and so make it watertight. The cap was pressed on to the bottom of the duck so as to snap into position over a

flange on the duck itself and this was intended to hold it tight and as waterproof as possible.

The order for 18,000 units was filled by All Plastics promptly and delivered to Eunick. Some problems emerged at once. The individual spheres were packed in a small carton and 24 of these were packed in a larger carton for delivery purposes. When they arrived at Eunick's premises it was seen that some of the cartons were damp. It was soon recognised that there was a problem over the inadequate sealing of the two halves of the spheres. The defective balls were returned to All Plastics and replaced by them. There were also some returned from customers but the number was not so high as to be regarded as a major problem. It should be noted that the only defect which had appeared at this stage was that of leaking.

Once the first order of 18,000 units had been disposed of Mr Curtis wished to order more but he wanted to overcome the difficulty as to leaking. It had been found that the K Resin material did not adequately stand up to tests and was inclined too readily to break. Some investigation was therefore carried out on the Greek product and it was found this had been made of a substance called Cellulose Acetate. Both Mr Curtis and All Plastics considered the Cellulose Acetate would be a preferable material but there are different types and grades of Cellulose Acetate and here a further point of difference arose. Having regard to the enquiries they had made All Plastics considered that they should use the form of material made in Germany and known as Cellulose Acetate Butyrate (CAB). Mr Curtis had made his own investigations and considered that an English product which was referred to simply as Cellulose Acetate was preferable. This was for two reasons. The first was that it was cheaper, and the second that it was readily available through a supplier in

Auckland and did not involve waiting for a shipment from Germany. Mr Billing became very upset at Mr Curtis's refusal to agree to the use of CAB and his attitude over this may well have accounted for some of the difficulties which developed between the parties. It is not altogether clear why Mr Billing should have been so adamant about this because there is not, as I understood it, any suggestion that the use of the English material resulted in any defects or was responsible for the principal matter in dispute. There was some discord also over the type of glue to be used in order to join the two halves of the sphere, but it was conceded by Mr Billing, in evidence, that the glue specified by Mr Curtis was adequate for the job so long as it was correctly applied. The question of the type of material to be used for the spheres gives rise to the main defence offered by All Plastics and requires particular consideration later.

In the end agreement was reached and a second order was placed with All Plastics. This was written out by Mr Maguire on Eunick's printed form on 1 May 1981 and was for the manufacture and supply of 12,500 Roll-a-Duck units and also 12,500 Butterfly balls. The latter comprised a different product which was the subject of a separate transaction between the parties and with which I am not concerned. The time for delivery of the Roll-a-Duck units was expressed to be between 1 and 5 June 1981. In the result there was a delay for reasons which have no present relevance and deliveries did not start until about July and went on until November 1981. It is this second order which forms the basis of the present action.

The order of 12,500 units was never completed. Although a total of 14,081 units were manufactured and delivered, 3,682 were subsequently returned as defective. There were orders from retailers waiting to be filled.

particularly as the time of delivery of this second order coincided with the time retailers were stocking up for the Christmas trade. Consequently, as quickly as supplies were received by Eunick from All Plastics they were sent out to retailers. It was not long before they were being returned in substantial numbers. In some cases this was because of leaking but now a new problem appeared. It was, at first, not clear what the cause of the problem was, but eventually it became apparent that it was due to the washers having rusted. This resulted in discolouration of the water so that the toy became most unattractive in appearance. As I have said, 3,682 units were returned to All Plastics and a credit was given to Eunick for them. These had been defective for different reasons. Some had leaked, some had been found to have a white line round them due to an excessive quantity of glue, and some had discolouration due to rust. This was not the total of the balls returned to Eunick as many more were received after the credit referred to had been given. Of those further balls returned the majority were defective because of the effects of rust.

The result was that Eunick looked to All Plastics for compensation and All Plastics declined liability. The present action was then commenced. Although there have been a number of matters of discord between the parties, the present claim concerns a fairly narrow issue. It relates to a claim in respect of all the Roll-a-Duck balls supplied under the second order for which credit has not already been given. The basis of the claim is that they were defective either because they leaked or, more particularly, because of the rusting of the washers. The defence to this claim is, in essence, that Eunick agreed that All Plastics should be under no liability in respect of the product manufactured and supplied by it and, alternatively, that there is no liability in any event because All Plastics has done no more than comply with the specifications of Eunick. In the

course of the hearing Mr Billing conceded, on behalf of All Plastics, that to the extent that any of the spheres leaked this would be because of defective workmanship and would be the responsibility of All Plastics.

The plaintiff's claim, as pleaded, is based upon breach of contract and, in the alternative, negligence. But it was conceded that the present state of the law did not allow both causes of action to be pursued and so the case proceeded on the allegation of breach of contract only.

There are several particular matters which required consideration:

1. Whose was the responsibility for the rusting of washers?
2. Did Eunick agree that All Plastics should bear no responsibility for the product?
3. Do the provisions of the Sale of Goods Act 1908 apply?
4. Damages.

1. LIABILITY FOR RUSTING

In discussing this topic I do so without reference to the question of general responsibility for the product which is the subject of the second topic.

What is clear is that the defect which has formed the subject of the majority of the Roll-a-Duck balls supplied under the second order was the result of water reaching the washers so that the consequent rusting

discoloured the water. Some attempt was made to argue that it was not clear whether the balls returned to Eunick because of this defect came from the first or the second order. It would obviously be difficult for that to have been determined with precision in every case. On the balance of probabilities, however, it seems clear that none of those now in issue related to the first run. This was a product in heavy demand and was being sold as soon as it was distributed. The first order of 18,000 units was delivered by about October or November 1980. There was then a gap while the negotiations went on with regard to the second order. The first of those was not delivered until about July 1981. If any of the first order had been defective by reason of rusting, one could have expected this to have become apparent well before the second order came on the market. The first signs of rusting appeared not long after the second order was distributed and it seems most unlikely that this related to any of the first order.

It is also of significance that there was no complaint of rusting with any of the product manufactured by Electroformers. The problem with those units concerned water getting into the ducks but even then the complaints were few. Rusting was a new problem and it was confined to the second order from All Plastics. This is of some importance because it was All Plastics who decided that Electroformers' method of using Dum Dum was unsatisfactory and needed changing. On behalf of All Plastics it was said that the use of Dum Dum had been for the purpose of sealing the hole in the bottom of the duck and not in order to stop water reaching the washer. Both Mr Billing and Mr Collier were adamant that nothing could have stopped water reaching the washers and that Dum Dum would certainly not have had that result.

I am not at all satisfied that either assertion is correct. Results seem to indicate that both the Greek manufacturers and Electroformers had been successful in preventing water reaching the washers. The Greek method was to encase the washers in a plastic sachet. The Electroformers method was to use Dum Dum. If either method had proved unsuccessful one would expect to have seen some evidence of it, but there was none. It is not really crucial to a decision in this case but I should have thought that the continued use of Dum Dum would have afforded protection for the washer and perhaps avoided the rusting problem from arising. The decision to change the method was that of All Plastics. This at once suggests that the responsibility for the substitute method is likely to be their's.

Considerable stress was laid by All Plastics on the fact that nearly all the aspects of manufacture were specified by Eunick. This was certainly so. Without going into them in detail it may be said that Mr Curtis acknowledged he had specified K Resin for the first order and the English variety of Cellulose Acetate for the second; he had specified the use of water containing a particular quantity of Nipogen inside the spheres; he had specified the shape and colours of the ducks; and he had specified that there should be galvanised metal washers. It was accordingly argued that All Plastics were required to do no more than manufacture in accordance with those specifications and that they had done so. They themselves had indicated a preference for plastic or stainless steel washers but both had been rejected by Mr Curtis. This was partly on the ground of cost and, in the case of plastic washers, because there would be insufficient weight to keep the ducks upright. The case cannot, I think, be resolved merely by reference to the fact that in the end Mr Curtis specified the use of galvanised washers. It cannot be the

case that the use of galvanised washers of any quality at all, however inferior, would absolve All Plastics from liability. They were the manufacturers and their responsibility extended further than that, particularly in view of the fact that they had rejected the use of the Dum Dum material and had left the washers without any protection from water save only the extent to which the cap fitted tightly on to the duck.

The evidence was that there are two principal forms of galvanising. One is by an electrolytic process which deposits a thin layer of zinc on the metal. The evidence of a scientist was that this would resist water for only a few months. The other is known as the "hot dip" process which involves immersing the metal in zinc so that a fairly substantial coating of zinc is applied. It is obvious that the latter method is likely to be more effective and long-lasting than the former and the scientist's evidence was that this would resist water for a number of years at least. On behalf of All Plastics it was argued that they may have been experts in plastics but were never to have been regarded as experts in metal products and so could not have been expected to appreciate the difference between the two methods. This argument may have had some force had it not been for the concessions made in evidence by Mr Billing.

He was resistant to any suggestion that he had a responsibility to choose from the available methods and said that it had been a matter of the method which happened to be used by the firm to which the washers were sent. He acknowledged, however, that he was aware of the difference between the two methods and knew that hot dipped washers would resist rusting for much longer because of their thicker coating. He acknowledged, also, that he knew he was dealing with a customer who was concerned at the possibility

of rusting and that, in the end, the choice as to the method of galvanising was his. In view of his knowledge and his firm belief that it was not possible to prevent water reaching the washers there was, in my view, a clear responsibility on him to see that the specified galvanising was carried out by the more resistant of the two methods known to him. It appears that some of the washers used were indeed galvanised by the hot dip method. No doubt this applied to those used on the first order and accounts for the absence of complaints of rusting in respect of that order. All Plastics then changed to another firm and evidently the less effective method was used with the results which occurred in the second order. In the absence of any other consideration I therefore conclude that the liability for the rusting was that of All Plastics.

2. THE DEFENCE OF EXONERATION FROM LIABILITY

This defence arose out of the account given by Mr Billing of a discussion with Mr Curtis and Mr Maguire on 15 April 1981. That was the occasion on which a second order was discussed and when the matter of the material to be used for the spheres was canvassed. I have already said that, in the face of Mr Billing's advice that the German material was preferable, Mr Curtis stipulated that it should be the English material for reasons of cost and availability. Mr Billing conceded that he was very angry at this decision and became very heated about it. His evidence was that he accordingly resolved to accept no responsibility for the product. During the course of the meeting Mr Collier, who was also present, made some notes in his diary and, in particular, he recorded - "Richard supply material, accepts all responsibility for product." Richard, of course, refers to Mr Curtis. This was the basis of Mr Billing's assertion that Mr Curtis had absolved All Plastics from any liability

in respect of defects of any kind occurring in the Roll-a-Duck balls.

This assertion is plainly untenable and I am not prepared to accept it. There is no dispute over the fact that Mr Curtis insisted on the use of English Cellulose Acetate and that he accepted responsibility for problems which may arise out of the use of that material. He has acknowledged as much. But that is altogether different from an acceptance of responsibility for the entire product in all its respects. Plainly no such concession was made. Of particular significance in this regard is that Mr Collier's recollection of what was intended differs from that of Mr Billing and is consistent with that of Mr Curtis. He was asked in his examination-in-chief, "Tell us in your own words what you thought what All Plastics had opted out of?" And he replied, "Anything to do with the failure of the Cellulose Acetate in the Roll-a-Duck ball." He later made an attempt to qualify this by saying that it really extended to an exoneration of liability in respect of the use of galvanised washers but it was plain that he was referring to a separate occasion and that he was anxious to combine the two in order to change the effect of what he had earlier said. However, whether that is so or not, I am satisfied that there never was any complete exoneration of liability by Mr Curtis in respect of the entire product. As he put it, he would have been crazy to have done any such thing and I am sure he did not do so.

Another matter requires consideration under this general heading of exoneration of liability. I have referred previously to Eunick's printed form of order which was used in respect of each of the two orders placed. That form has, on the back of it, a set of conditions which are said to apply to the contract. Those conditions are in familiar form and are designed to limit or exclude the

liability of Eunick as far as possible. Mr Billing said that when he saw these conditions on the occasion of the first order he took strong exception to them and rang Mr Maguire to tell him that in no circumstances would he agree to accept the order on the basis of those conditions. He said that Mr Maguire responded that if he did not want to accept them he need not. Mr Maguire denied that any such conversation took place. The matter is probably of little relevance because the plaintiff's case has at no stage been conducted upon reliance on any of the conditions on the back of the contract. In case it should be thought to have any real significance, however, I should say that I accept Mr Maguire's evidence in preference to that of Mr Billing. Mr Maguire was the most independent of the witnesses but, in any event, I found him the most reliable and convincing.

Some point was made over the fact that in respect of neither of the written orders did All Plastics complete and return to Eunick a carbon copy, as they were expected to do, in order to signify acceptance of the order. The evidence was vague as to whether this was a particular requirement of Eunick, and the carbon copy in question was not produced in evidence so I am unaware whether it has something on it specifying, for instance, that the order would not be regarded as accepted unless it were signed and returned. Mr Maguire's evidence was that, as a matter of general practice, it was more common for the carbon copy not to be returned than for it to be returned. The point is, I consider, of little relevance because the order was in fact accepted by All Plastics and in part, at least, carried out.

3. THE SALE OF GOODS ACT

In the course of his final address Mr Chapman, on behalf of Eunick, sought to rely upon a submission that the

Roll-a-Duck balls manufactured by All Plastics were not of merchantable quality and he placed reliance upon a concession made in cross-examination by Mr Billing that those balls which had leaked or in which the washers had rusted were not of merchantable quality. Mr Reed, for All Plastics, argued that there had been no pleading in the amended statement of claim based on the Sale of Goods Act and that the submission was not available to Mr Chapman. This seems to me to be correct. It is not, of course, necessary to plead the law, but a proper basis of fact must be pleaded in order to establish that a cause of action exists to which a matter of law may be applied.

The plaintiff's case, as it appears from the amended statement of claim, is based upon an allegation of breach of contract. The only pleading which might be regarded as raising a cause of action under the Sale of Goods Act is para 7:

" 7. AFTER delivery to and subsequent resale by the plaintiff of the said toys the plaintiff received notice that the said toys were defective in that:

(a) The water contained in the plastic spheres became discoloured; and

(b) The plastic spheres leaked;

thereby rendering the said toys unmerchantable. "

In the course of the hearing various references were made to the question of whether the balls were of merchantable quality. The fact that they were not does not of itself amount to a cause of action. The only part of s 16 of the Sale of Goods Act, which refers to merchantable quality, is para (b):

" 16. Subject to the provisions of this Act and of any statute in that behalf, there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods supplied under a contract of sale, except as follows:

(b) Where goods are bought by description from a seller who deals in goods of that description (whether he is the manufacturer or not), there is an implied condition that the goods shall be of merchantable quality:

Provided that if the buyer has examined the goods, there shall be no implied condition as regards defects which such examination ought to have revealed. "

That provision can have no application in the present case as there is no suggestion that this was a purchase by description by Eunick. I am, therefore, not prepared to consider the case in terms of the Sale of Goods Act.

4. DAMAGES

The plaintiff has claimed \$28,157.02 by way of special damages, together with interest on that sum and also \$20,000 for general damages.

The basis of the claim for special damages was set out in a schedule produced by Mr Barnaby, Eunick's Secretary and Accountant. As I understood it, his calculations were challenged only in respect of two main matters. One was that in arriving at the calculation of loss Mr Barnaby had failed to take into account a proportion of overhead expenses for the whole business and to debit that proportion against the expected profit on the Roll-a-Duck balls. This was not, in my view, a valid

objection. The estimate of loss was arrived at by calculating the nett profit which would have been received if the contract had been fully performed and adding the calculation of loss actually incurred. If a proportion of overheads ought to have been deducted from the first figure then the same proportion would need to have been added to the second. The two amounts are not identical but plainly the amount involved would be small. Whether a proportion of overheads would have been capable of calculation I am not sure, but I cannot see that the final figure arrived at would have been different to any significant extent from that arrived at.

The other criticism was that, to the extent that the defects related to leaking, the balls had been replaced by All Plastics and that it had not been shown that all the remaining ones, upon which the calculation of loss was based, were defective because of rusting. In part, this was a submission that some of the rust-affected balls may have come from the earlier order. I have already dealt with this. It must be accepted, however, that it was not possible for Eunick to establish that every one of the balls supplied under the second order was defective. Mr Barnaby's figures, which were taken from Eunick's records, showed that a total of 14,081 units were supplied by All Plastics under the second order. Of these 3,682 were returned and a credit given for them. This leaves 10,399. According to Mr Curtis's evidence 5,040 were sent to Australia and when it was found they were defective they were all destroyed in order that a refund of duty could be obtained. The balance were distributed on the New Zealand market and of these about 4,000 were returned. These figures are not precise, but they show that at least a few hundred have not been returned and may, for that reason, not have been defective. Although no precise calculation can be made I think some

allowance must be made for those units which were probably not defective.

In this situation I can do no more than make an arbitrary assessment based upon the figures supplied. Bearing in mind the onus of proof, I think I ought to make that assessment on a conservative rather than a liberal basis. Looking at the matter in this way I find that special damages of \$24,000 have been established. Interest on this sum at 11% per annum must also be allowed. Interest is claimed as from 1 January 1982. As payment will have been made by Eunick prior to that date I am prepared to adopt 1 January 1982 as a reasonable date from which interest should run.

There remains the claim for general damages. This was based, primarily, upon the loss of orders for the product and damage to Eunick's goodwill. These are matters which cannot readily be assessed. Following the result of the second order placed with All Plastics, Eunick has done its own manufacturing. The machinery was ordered in January 1981 and manufacturing commenced at about the end of June 1981. Eunick was therefore in a position to supply the market before it had received the second order from All Plastics. Mr Curtis gave evidence as to the product which was being produced. This had some changes from that specified to All Plastics but in appearance is substantially the same article. Mr Curtis said his new product was selling well but that, because of the defects in the units produced by All Plastics, there had been a period of about six months when the product was off the market. By the time the new product appeared the toy had lost its novelty and also Eunick had lost some of its retail outlets because some large firms would not accept the Roll-a-Duck balls after the experience they had had with the defective ones.

I have had some difficulty reconciling Mr Curtis's evidence that his new product is selling well with his claim for loss of goodwill, but I accept it is probable that a certain market resistance would have needed to be overcome and may, indeed, have continued. I do not think any large sum can properly be awarded for general damages, but that a case has been established for a modest amount to meet the considerations to which I have referred. I am prepared to award \$3,000 for general damages.

In summary, therefore, there will be judgment for the plaintiff for \$24,000 for special damages with interest thereon at 11% per annum from 1 January 1982 to the date of judgment, and for \$3,000 for general damages. The plaintiff is also entitled to costs according to scale, with disbursements and witnesses' expenses as fixed by the Registrar. I certify for two extra days at \$300 each and \$100 for discovery and interrogatories.

Solicitors: Roache, Cain & Chapman, WELLINGTON, for
Plaintiff

Scott, Morrison, Dunphy & Co., WELLINGTON, for
Defendant



