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Paper by
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Implications of lending to an unexpected issuer of securities: Hickman v Turner & Waverley and GE Custodians v Bartle.

The difference of perspective: *Hickman* in the Supreme Court

Liam Mason[1]

The New Zealand Supreme Court's decision in *Hickman & Ors v Turner & Waverley Limited*[2] should not have been surprising. Judicial commentary has, since the earliest days of the legislation, emphasised the breadth of the definition of "security" in the Securities Act 1978. Drawing on the underlying policy of this law the Supreme Court applied a literal reading of the definition of "debt security" to come to a different conclusion to that of the Court of Appeal and the High Court, and to find that the investment products offered by Blue Chip New Zealand Limited involved an offer of debt securities to the public. Applying an expansive approach to the legislation's allocation of responsibility for offers of securities, the Court also concluded that the developers who were selling the underlying real estate interests were, along with the Blue Chip companies, "issuers" of the securities. The result was that the sale and purchase agreements by which the investors had committed to purchasing apartments were themselves unenforceable.

The Supreme Court's judgment confirms that the broad language of the Securities Act should not be read down where its plain application would be consistent with the underlying policy of the law. While this instruction should appear trite, the Court of Appeal's judgment in this case reflected a reluctance to do that, driven by a concern that to do so would extend the law beyond its intended bounds. In finding that the result achieved was consistent with the underlying purpose of the legislation the Supreme Court demonstrated the difference in outcome that can be achieved if an investment transaction is viewed, as it should be under this legislation, from the point of view of the investing party and if the economic substance of the transaction as it concerns that party is given primacy when assessing the legal consequences of the various agreements that form the transaction.

The Blue Chip products

[1] Views expressed in this paper are those of the author, and should not be taken to reflect the views of the Financial Markets Authority.

2 [2012] NZSC 72

Blue Chip New Zealand Limited was established in 2000, offering investment products based on residential property. These products were marketed as providing cash flows for investors who could participate by making use of “dormant” equity in their existing properties. The company’s 2005 annual report, cited in the High Court judgment, stated:

> *“Blue Chip New Zealand’s point of difference remains providing a financial planning solution that utilises property, rather than just providing a property itself…Investors know up-front the returns to expect, which is more akin to a financial product than a standard property investment.”*[3]

As it turns out, that is precisely what the Supreme Court thought.

Blue Chip entities marketed a number of different investment products.

Mainstream product

The mainstream product was at issue in the High Court and Court of Appeal, but not the Supreme Court. An investor in the mainstream product purchased a residential apartment from a developer, subject to a deed of lease with a Blue Chip entity, with the rent guaranteed by Blue Chip NZ Ltd. Investors also purchased a furniture pack and entered into property management agreements with another Blue Chip entity.

Joint Venture product (JV)

Investors in the joint venture product also agreed to purchase an apartment from a developer and a furniture pack. In addition, they entered into an agreement with a Blue Chip entity, Blue Chip Joint Ventures Limited, to establish a joint venture company to engage in the business of owning and leasing the apartment. The investor was responsible for providing the equity by which the joint venture could purchase the apartment, including a contribution for working capital. The Blue Chip entity was responsible to meet the costs of any borrowing and to pay to the investor a fortnightly procurement fee.

The joint venture was to continue until wound up unless the parties agreed to sell the property or terminate the joint venture. In the event of a sale of the property any net proceeds would be split 95% to Blue Chip, 5% to the investor. It was intended that these investments would last for approximately four years.[4] Should

[3] Blue Chip New Zealand Limited 2005 annual report, cited in *Hickman & Ors v Turn & Wave Limited & Ors* HC Ak CIV-2008-404-005871 [9 December 2009], Venning J at para 23.
[4] Above, no. 2, at 38.

the joint venture be wound up, the investor would receive 100% of the net proceeds of the sale.

Premium Income Product (PIP)

In addition to the apartment and furniture pack, PIP investors granted an option to Blue Chip Premium Income Limited that allowed Blue Chip to step in to purchase the apartment (before or after settlement). The investor was paid a monthly option fee by Blue Chip.

The PIP agreement provided that if the option were not exercised the sale and purchase agreement would be binding on the investor. Should the investor be required to settle in the property purchase, the PIP agreement provided that Blue Chip would pay the settlement costs (excluding the purchase price) including the interest costs on any borrowing relating to the settlement and would also procure lease arrangements similar to those for the mainstream product.

Put and Call Agreement Product (PAC)

As the name suggests, the essential feature of the PAC product was that it involved a put option by which the investor could require Blue Chip to acquire the apartment, in addition to a call option by which Blue Chip could step in to purchase. The investor again received a monthly option fee for the call option granted to Blue Chip.

The Securities Act 1978

This case concerned investment products marketed by Blue Chip entities in conjunction with purchases of apartments from separate development companies. With one exception the development companies were independent of the Blue Chip entities. The investment products had seen investors borrow heavily against their existing homes to finance purchases of apartments, with promises that Blue Chip entities would cover most of the financing costs and at least an understanding in many cases that investors would not be required to settle on their purchases.

The Blue Chip group went into liquidation in early 2008, leaving investors without their promised returns. The property developers, meanwhile, sought to enforce the sale and purchase agreements on the apartments. The investors argued that these were unenforceable.

By the time the case reached the Supreme Court the remaining issues were whether the marketing of the Blue Chip investment products contravened the Securities Act, and whether as a consequence the sale and purchase agreements for the apartments were unenforceable.

The case turned on a number of features of the Securities Act.

Debt Security

The Securities Act defines a debt security as:

> *…any interest in or right to be paid money that is, or is to be, deposited with, lent to, or otherwise owing by, any person (whether or not the interest or right is secured by a charge over any property); and includes–*
> *(a) a debenture, debenture stock, bond, note, certificate of deposit, and convertible note; and*
> *(b) an interest or right that is declared by regulations to be a debt security for the purposes of this Act; and*
> *(c) a renewal or variation of the terms or conditions of any such interest or right or of a security referred to in paragraph (a) or (b)…*

Put simply, the investors' claim was that because the various Blue Chip products involved promises of payment of money to investors, they fell within the definition of "debt security".

Issuer

The Securities Act applies to securities offered to the public by or on behalf of the issuer of those securities. In respect of debt securities, "issuer" is defined as "*the person on whose behalf any money paid in consideration of the allotment of the security is received*".

Importantly to the result in the Supreme Court, "money" in the Securities Act is defined to include money's worth.

Real estate exception

Section 5 of the Securities Act contains a number of statutory exemptions from the operative provisions of the Securities Act. One of these, in section 5(1)(b), states that the compliance provisions of Part 2 of the Act do not apply:

> *…in respect of–*

> (b) *any estate or interest in land for which a separate certificate of title can be issued under the Land Transfer Act 1952 or the Unit Titles Act 2010, other than any such estate or interest that–*
>
> *(i) forms part of a contributory scheme; and*
>
> *(ii) does not entitle the holder to a right in respect of a specified part of the land for which a separate certificate of title can be so issued…*

There was no dispute in this case that sale of the apartments themselves amounted to the sale of estates or interests in land. However, the 1996 decision of the Privy Council in *Culverden Retirement Village Ltd v Registrar of Companies*[5] had established that different aspects of a transaction could be considered separately for the purpose of assessing the need to comply with the Securities Act. If a provision in a transaction involved an offer of securities other than the offer of an estate in land then the exemption in section 5(1)(b) would apply only where the provision in question could be described as ancillary to the purchase of the land.

The effects of non-compliance

The Securities Act prohibits any offer of securities to the public by or on behalf of an issuer unless there is a registered prospectus for the securities. In the case of an offer of a debt security the issuer must appoint an authorised trustee and execute a trust deed. These obligations are largely self-enforcing, as section 37 of the Act provides that no allotment of a security offered to the public may be made if there is no registered prospectus. Section 37(4) provides that any such allotment is "invalid and of no effect". Section 37(5) states that any subscriptions received "by or on behalf of an issuer" in such a case must be repaid to the subscribers.

The High Court decisions

Three sets of proceedings were taken in the High Court, against three developers:

> Greenstone Barclay Trustees Limited (Greenstone)
> Turn and Wave Limited (TWL)
> Icon Central Limited (Icon)

The proceedings in the High Court sought relief for the investors under the Fair Trading Act 1986 and on the basis of contractual misrepresentation, as well as under the Securities Act. The claims under the FTA and contract required the Judge, Venning J, to undertake a close analysis of the various agreements between the

[5] [1997] 1 NZLR 257 (PC)

developers and the Blue Chip entities, in order to establish whether any misrepresentations made by the Blue Chip companies were made as agents of the developers. A central claim of the investors in relation to these causes of action were that the Blue Chip representatives made misleading representations about the Blue Chip investment products, and did so as agents of the developers.

The High Court judgments set out a close analysis of the various contracts between investors, Blue Chip companies, and the developers. Venning J distinguished between those Blue Chip companies that had specific obligations as underwriters and other members of the Blue Chip group. He concluded that while certain companies were agents of the developers, this agency existed only for the purpose of selling apartments, not for the sale of Blue Chip investment products. The Judge also gave weight to "entire agreement" clauses in the sale and purchase agreements, which sought to exclude liability for the developers for any representations not set out in the agreement. Although such clauses would not allow the developers to contract out of the FTA, the Judge found that the clause could operate to limit the developers' liability to representations concerning the apartments themselves (as there was no agency granted by the developers to sell anything else).

As to the application of the Securities Act, the Judge observed that most commercial property purchases are made to obtain access to cash flows from rental income. This is not sufficient to make the offer of such property, even with a lease in place, the offer of a security. The Judge observed also that the right to a rental stream under the lease is not acquired by virtue of contract or the offer of a security but by operation of law, under the Property Law Act. On this basis the mainstream product did not involve an offer of securities.

The investors argued that the JV product involved an offer of both debt securities and equity securities. While expressing some reservations as to why Parliament would require the appointment of a trustee and creation of a trust deed in such a situation, Venning J accepted that on the basis of the Privy Council's decision in *Culverden* there was a basis for the argument that the payment of the procurement fee and the reimbursement of borrowing costs could be seen to be a right to be paid money that is, or is to be, owing by, the Blue Chip entity. He was also prepared to accept that the Blue Chip entities could be issuers in these circumstances, given that the JV agreement required the payment of substantial sums of money to the Blue Chip entity, quite apart from the deposit on the apartment.

There was, however, no need to take a firm view on these points, as Venning J was clear that the exception in section 5(1)(b) did apply in this case. As the Judge saw it:

> *the substance of the transaction created by the joint venture agreement is the purchase and ownership of the apartment by the joint venture partners. The repayment of the borrowing costs and the payment of the procurement fee are part of the joint venture agreement, which is directed at the purchase of an interest in land…The features that the plaintiffs characterise as debt securities can properly be said to be ancillary to the purchase of an interest in land…*

As such, these payments were found to be "in respect of" the exempted interest in land, and so covered by the exemption in section 5(1)(b).

In respect of the PIP and PAC products the High Court observed that the only money paid by an investor was the deposit on the apartment. This was not, in the Court's view, received "by or on behalf of" any Blue Chip entity, even if "on behalf of" was given a broad definition, to mean "for the benefit of". Accordingly even if the Blue Chip entities were offering rights to receive money, they were not the issuers of any debt security, as there was no consideration for the allotment of the security received by or on behalf of Blue Chip entities. Consistent with the finding in relation to the JV products, the Court found that in any event the payment by Blue Chip of an option fee was clearly in respect of an interest in land that was exempted by section 5(1)(b), as was any right to reimbursement of the deposit.

Court of Appeal

In the Court of Appeal the three cases were combined. Only the Securities Act claims were pursued.

The Court of Appeal reached the same conclusion as the High Court, in a decision delivered by Randerson J. The Court noted that the Court of Appeal's decision in the *Culverden* litigation had set out the following approach to interpretation of the term "debt security" in the Securities Act:

> *The scheme of the Act appears to cast the net in the widest possible terms, and then to rely on specific exclusions to limit its scope…We see no reason to read down the wide language of the definition.*

Despite reminding itself of this, the Court was unable to accept that the money flows and obligations created by the Blue Chip products were what was contemplated by Parliament in the legislation. The Court agreed with counsel for the developers that the general words "any interest or right to be paid money that is …otherwise owing" needed to take colour from the other terms included in the definition, including the

references to deposits, loans, debentures, and so on. In particular the Court of Appeal was troubled by the lack of any repayment of money in the obligations assumed by Blue Chip, concluding:

> *While, as* Culverden *attests, the definitions of security and debt security are widely expressed, we do not consider that Parliament intended the definition of debt security to embrace commercial transactions which do not involve some element of repayment of money subscribed by investors.*

This finding was by itself sufficient to dispose of the case, the Court examining each of the Blue Chip products and finding no instances where money owing to an investor could be characterised as repayment of a sum subscribed. This extended to the feature of the PAC product by which Blue Chip reimbursed an investor for the deposit paid on an apartment on exercise of the option; the Court observing that an agreement to pay to the investor a sum equivalent to that paid by the investor to a developer was not the same as repayment of a sum subscribed.

Had there been an offer of securities, the Court of Appeal was less convinced than the Judge at first instance that the offer would have been covered by the real estate exemption. Stressing that the transaction should be considered from the point of view of the investor, the Court was of the view that the Privy Council in *Culverden* had been referring to "normal agreements for sale and purchase of land with no unusual features" when considering whether a right acquired under one element of a transaction was ancillary to the interest in real estate and thus exempt. On this basis the Court applied a two-step consideration: (i) was the feature merely ancillary or a cardinal feature and (ii) was it an unusual feature in terms of an agreement for sale or purchase of an estate or interest in land.

Applying this approach, the Court saw the payment of the procurement fee in respect of the JV product to be an "essential or cardinal" feature of the transaction. Investors had no expectation of anything other than a modest share of any capital gain from the property, leaving the procurement fee as the only material return that they would receive. The fee was "of the essence of the investment" and was also an "unusual" feature, not one that could be seen as a normal element of a sale and purchase agreement or even of a joint venture in respect of an estate or interest in land.

Applying the same two step reasoning to the PIP product resulted in the Court distinguishing between the option fee payable to investors and the obligations on Blue Chip to pay settlement costs if the option were not exercised and to reimburse the deposit amount if the option were exercised. The Court of Appeal noted that the obligation to pay the option fee was conditional on the investor entering into the

sale and purchase agreement for the apartment, and was payable in return for the grant of an option that was itself an interest in land. On this basis the Court concluded that the payment of the option fee, while an important feature of the transaction, could not be regarded as unusual. The agreements to pay settlement costs or to reimburse the deposit, however, were considered to be "both critical and unusual" aspects of the PIP agreements. The Court reached the same conclusion in respect of the option fee and reimbursement obligations under the PAC product.

In passing, and relevant to the mainstream product, the Court of Appeal, like the High Court, did not think there was any doubt that the rental stream payable under a lease was a right "in respect of" an estate or interest in land.

The Supreme Court

In the Supreme Court, Elias CJ, McGrath, and Anderson JJ joined with the reasons given by William Young J, while Tipping J delivered a concurring judgment that further explored the application of the common law doctrine of tainting. The Court was unanimous in finding that the Blue Chip products were debt securities offered in breach of the Securities Act, that the sale and purchase agreements were unenforceable as a result of that breach, and that the developers were also issuers (with Tipping J also finding that the sale and purchase agreements would be unenforceable as a result of tainting).

How did the result in the Supreme Court depart in almost every respect from those in the lower Courts? The answer, it is suggested, shows the difference of perspective. The careful analysis of the various agreements by the High Court and the Court of Appeal had begun in each case with the sale and purchase agreements, and had treated the Blue Chip products as extensions or additions to these agreements for the sale and purchase of real estate. By contrast, the Supreme Court from the beginning approached the entire set of arrangements from the point of view of the investors:

> *The appellants participated in investment schemes marketed by the Blue Chip group of companies. These required them to commit to the purchase of apartments in one or more of three proposed developments on land which had originated with entities associated with Blue Chip but which, in two cases, had by then been sold to independent third party developers…*

The Supreme Court saw the transactions as part of a broader four-stage strategy run by Blue Chip, involving the company:

(a) identifying and securing sites that were suitable for development;

(b) either selling these to independent developers to build an apartment building or itself setting these arrangements in train;

(c) selling apartments off the plans to short-term investors to generate the pre-sales needed to secure draw-down of development funding (and at the same time producing underwriting fees for Blue Chip); and

(d) in due course, locating a second purchaser for each apartment to take out the initial investor.[6]

The case in the Supreme Court involved only the JV, PIP, and PAC products. Viewed from the perspective of the investors in these products, the benefits sought were associated with cash flows to be provided by Blue Chip, not from the inherent value of the apartments being purchased under the sale and purchase agreements. Viewed from their place within the broader Blue Chip strategy, the role of the investors was to finance Blue Chip's own acquisition of the apartments (for resale under its mainstream product).

This investor-centric view of the transactions, together with a plain-reading approach to interpretation of the Securities Act, supported by its statutory policy and context, required a very different result from that reached in the Courts below.

New Zealand Courts have long held that the application of the Securities Act must be approached from the point of view of the investor.[7] The Supreme Court's decision in *Hickman* demonstrates the difference it makes when a Court rigorously applies this to a series of linked transactions.

Debt Security

The Court of Appeal had addressed this central issue, in essence, by finding that the notion of "debt security" necessarily involved some element of repayment by an issuer. The Supreme Court traversed the history of the Securities Act, noting its connections to securities legislation in the US, Canada, and Australia, in particular similarities between the broad scheme of the New Zealand legislation and the equivalent provisions of the Companies Act 1961 (NSW), taking support from the plain reading given to the provisions of that law by the High Court of Australia in *Australian Softwood Forests Pty Ltd v Attorney-General for the State of New South Wales; ex rel Corporate Affairs Commission*[8]. The Court observed that the primary provisions of the Securities Act would be "unacceptably broad" in scope were it not

[6] Above n.1, at [7].
[7] *DFC Financial Services v Abel* [1991] 2 NZLR 619 (HC)
[8] (1981) 148 CLR 121.

for the fact that the legislature had provided specific statutory exemptions (including the exemption for interests in real estate) as well as scope for the definition of "security" to be limited by regulation and a further power for the Securities Commission to exempt any person or class of persons from the operation of the Act.[9]

The leading case on the definition of "debt security" prior to *Hickman* was the decision of the Privy Council in *Culverden Retirement Village v Registrar of Companies*.[10] That case concerned a retirement village which offered freehold interests (under the Unit Titles Act) in units, on terms requiring residents to resell their units to the operator of the village when they were no longer needed. At all levels the Registrar of Companies was successful in arguing that the offer of the buy-back right in association with the unit resulted in an offer of debt securities that was not covered by the real estate exemption in section 5(1)(b).

The Supreme Court in *Hickman* focused its analysis on the judgment of the Court of Appeal in *Culverden*:

> *Mr Judd QC for Culverden submitted first that the buy-back provision was not a debt security. The definition of "debt security" is "any interest in, or right to be paid money that is, or is to be, deposited, lent, or otherwise owing by any person". He submitted that the words "otherwise owing" should be read as covering only transactions of a similar kind to a deposit or loan. It should be read as coloured by its context, and as referring only to financial transactions involving a money consideration on both sides. Unless so read, he submitted, one would have the absurdity that an ordinary contract for sale and purchase of a dwellinghouse would create a debt security, as the vendor obtains the right to be paid money on settlement.*
>
> *The definition goes on to state certain transactions which are included and one which is not included. These are of little help in construing the earlier words. We agree that one would not ordinarily expect the term "debt security" to refer to an agreement for the sale and purchase of land. On the other hand, the words "or otherwise owing" are of the widest ambit, and they are not qualified in the definition itself. They are effectively qualified by the provisions of section 5. The scheme of the Act appears to be to cast the net in the widest possible terms, and then to rely on specific exclusions to limit its scope. An agreement for sale and purchase of a dwellinghouse or of other land is excluded, subject to a stated exception, by section 5(1)(b). We see no reason to read down the wide language of the definition.*[11]

[9] Above n. 1 at [46] –the judgment records that the Securities Commission's power to grant exemptions under section 5(5) of the Act is now repealed. While that subsection was repealed when the Securities Commission was disestablished in 2011, the exemption power was re-enacted in section 70B, now resting with the Financial Markets Authority.
[10] [1997] 1 NZLR 257 (PC)
[11] *Culverden Retirement Village v Registrar of Companies* (1996) 1 BCSLR 162 (CA)

The Supreme Court recorded that the Privy Council, when presented with the same repayment argument by the retirement village operator, “inclined to the view” that it was too narrow, but contented itself with finding that even on such an analysis the purchase of a unit along with a promise for repurchase did amount to a contract for the repayment of money previously paid to the operator by the unit holder, saying:

> *It was not repayment in the sense of repayment of a loan. But it was repayment in the sense of payment back of the same amount, subject to adjustment charges and inflation.*

The developers in *Hickman* argued that the *ratio* of the Privy Council’s decision in *Culverden* was consistent with an argument that a debt security exists only where there is mutuality of payment and repayment obligations between an issuer and a subscriber. The crucial difference with the Blue Chip arrangements, it was argued, was that the repayment (or payment) obligations fell on Blue Chip while the money subscribed by the investors was paid to a third party, the developers. It was suggested that this three-way transaction should not be characterised as a debt security.

The Supreme Court acknowledged this difference, but noted that if the underlying premise that the term “otherwise owing” must involve a notion of “repayment” were not accepted then it becomes difficult to justify why the term should be limited more generally to repayment of money paid by a subscriber to the issuer.

The Court added that the “tenor” of the Privy Council decision, despite its narrow *ratio*, strongly supported the investors’ arguments. This was certainly so in the case of the Court of Appeal decision in *Culverden*.

As the terms “deposited with” and “lent to” appeared in precursor legislation to the Securities Act it seemed clear to the Court that the words “or otherwise owing” must have been intended to add something to this. This conclusion was supported by the speech of the Minister of Justice on introduction of the legislation, which described the Bill that would become the Securities Act as defining securities “in a very wide sense”, intending to capture “less usual types of securities”.[12] Exactly what was added by the words “otherwise owing” was said to be at the heart of the case.

The Court rejected the argument that the term “otherwise owing” was intended to capture obligations that were “rather like” those of a borrower to a lender, describing such as test as impressionistic and leaving scope for “how long is a piece

[12] (14 December 1977) 416 NZPD 5339.

of string" arguments as to how much similarity should be required to engage the definition. Rather, the Court was content that a plain meaning construction was appropriate, consistent with the preferred approach of the Court of Appeal in *Culverden* and with the legislative history of the Securities Act.

Floodgates?

Just as had been the Court of Appeal in *Culverden*, the Supreme Court was faced with arguments that too broad an approach would open the floodgates to the application of the Act, leading to unworkable consequences. The particular example chosen by William Young J in the judgment is the argument that the Securities Act would apply whenever some offering of goods or service to the public carried the possibility that the offeror might have to pay money as a result of some defect in the goods or services or because they could not be provided.

Where such a right might arise in the context of the marketing of real estate, or other interests exempted under section 5(1) of the Act, the Court was confident that such liability would be so much an ordinary incident of the transaction as to be a right "in respect of" the exempted interest being offered, and so would be covered by the relevant statutory exemption.

Acknowledging that the statutory exemptions would not be a complete answer to the concern raised by the developers, as liability of this sort could arise in respect of rights for which there was no statutory exemption, the judgment focused instead on the fact that the regulated activity under the Securities Act is the *offer* of securities to the public. The Court reasoned that although liability for compensation in the event of fault or misrepresentation is a usual corollary of offering goods or services to the public, a person offering such goods or services cannot sensibly be said to be *offering* that right. The approach to be taken, according to the Supreme Court, is a "purposeful but non-technical construction of the definition of debt security":

> *So, on the purposive approach which we prefer, straightforward consumer transactions are not caught by the Securities Act concept of what is involved in offering debt securities to the public. On the other hand, on the same purposive approach, the phrase "otherwise owing" must be construed sufficiently broadly to be able to encompass what the Minister of Justice, when introducing the Securities Bill, called "less usual types of securities".*

The direction to examine a transaction to find what is actually offered is consistent with the investor-centric approach to the application of the Act taken by the Court and provides a straightforward means to avoid many situations where contingent

rights to receive money owing could otherwise require analysis in terms of the Securities Act.

Assessment alone of the right offered, however, is unlikely to remove some transactions that are clearly not intended to be caught by the legislation – such as where a straightforward consumer transaction, perhaps for the supply of some service, is offered with an explicit "money back guarantee". In such cases it would be hard to argue on a plain reading that the right to receive money is not offered to the public. Those situations, rather, will need to be construed by reference to the underlying purpose of the legislation, and an analysis of whether there is an investment purpose, from the point of view of the person being offered such a right.

Was Blue Chip an issuer?

The issuer of a debt security is the person on whose behalf any money paid in consideration for the allotment of the security is received. Central to the developer's argument in relation to the PIP and PAC products was that no money was paid to Blue Chip, so it was not an issuer. In consequence, it was argued, there was no breach of the Securities Act, which applies only to securities offered "by or on behalf of" an issuer.

In contrast to the Courts below, which had emphasised the legal obligations on investors to settle their transactions should Blue Chip not exercise its options, the Supreme Court here again looked at the substance of the transaction as presented to the investors:

> *The idea underlying the PIP and PAC agreements was that Blue Chip would, before or after settlement, take out the investors and in that way be credited (in relation to the developer) with any money paid by the investor. In this admittedly non-technical sense, the payments made by the investors to the developers were received on behalf of Blue Chip. Given the underlying purpose of the Securities Act we consider that a non-technical approach is the appropriate way to resolve this issue.*

This approach, which confounds the careful divisions created between Blue Chip and the developers by the contractual matrix, acknowledges that from the investors' point of view money was paid in return for an income stream from Blue Chip, with the intention that on "maturity" (exercise of the option) the capital (deposit) would be paid back to the investor. The fact that the literal cash flows involved a third party had little effect on the economic reality of the transaction from the investors' point of view.

The Court noted that it could arrive at the same conclusion via a different line of reasoning, relying on the fact that "money" under the Securities Act includes "money's worth". This allowed the entry into the sale and purchase agreements themselves as the consideration given by the investors, which conferred immediate benefits on Blue Chip in the form of underwrite fees and control over the apartments.

This latter analysis may have formed the genesis for the further conclusion, raised by the Court itself following the hearing, that the developers also were issuers of the debt securities offered by Blue Chip. The Court found this to be so because the consideration provided by investors for the Blue Chip products included their entry into the sale and purchase agreements. As such, the consideration for the allotments of securities, in the form of money (the deposits) and money's worth (the obligations under the agreements), were received by the developers, who were thus "issuers" under the Securities Act.

The Court appreciated the potential span of this approach, taking care to note that the notion of money being received "on behalf of" a person would not include those whose trade debts, incurred in relation to the supply of goods and services to an enterprise, are paid from money received by an issuer. It seems clear, however, that the approach to be taken to the phrase "on behalf of" in the context of the term "issuer" is to examine for whose benefit, in the context of the transaction as a whole, the money is being received, keeping in mind that this benefit may be shared between more than one person.

This undoubtedly broadens the notion of who is an issuer of securities for future cases. It may for instance resolve an ongoing question that arises in the case of "conduit" issuers as to whether the appropriate person to be identified as the issuer includes any upstream person for whose direct benefit funds are being raised or should be limited merely to the person who immediately receives subscriptions.

The section 5(1)(b) exemption

The perspective from which the Supreme Court approached the Blue Chip investments is most striking in its assessment of whether the statutory exemption for interests in land should apply to exclude the transactions from the operation of the Act.

In relation to the Blue Chip products themselves, the Court traversed US case law, remarking that the starting point under the Securities Act of 1933 is that the offer of

real estate as such, without any collateral arrangements, does not involve the offer of a security.

The extensive US litigation relating to real estate investments arises from the test enunciated by the Supreme Court in *Securities and Exchange Commission v Howey Co*[13], which established a test for determining whether an arrangement is an "investment contract", and thereby a security in terms of the 1933 Act. In that case the US Supreme Court defined an "investment contract" as an investment of money in a common enterprise with an expectation of profits solely from the efforts of others.[14] There is no equivalent in the New Zealand securities legislation to the concept of "investment contract". This was acknowledged by the Court in *Hickman*, which described the significance of the US cases as only contextual, but nonetheless significant in light of the common underlying purpose of the United States and New Zealand statutes.

The Court adopted the interpretation of section 5(1)(b) articulated by the Privy Council in *Culverden*. Disagreeing with the approach of the High Court and in part with that of the Court of Appeal, the Supreme Court held that it "could not seriously be suggested that the transactions entered into between the investors and Blue Chip in relation to the apartments…involved 'the ordinary purchase of land' or that the Blue Chip obligations to the investors were in the nature of 'an unexceptional term ancillary to the purchase of an interest in land'. The Court's prompt dismissal of the argument was reached, again, by viewing the bundle of transactions as a whole and from the point of view of the investor – to whom, if all went to plan, "the apartments were of only peripheral significance".

As the challenge being raised in the case concerned the obligations of the investors to now go through with settlement on the apartments to which they had committed as part of the investment, the Court separately considered whether the section 5(1)(b) exemption applied to the sale and purchase agreements themselves. Given that these were agreements for freehold interests in unit titles issued under the Unit Titles Act, they might, the Court recorded, be thought to fall "four square" within the exemption at first sight. This, in the Court's view, ignored the bigger picture. Investors subscribed for the Blue Chip products by entering into the sale and purchase agreements (among other things), and the operation of the Blue Chip products were inextricably associated with the sale and purchase agreements.

Noting that all of the developers had some degree of knowledge of the Blue Chip products, the Court found in any event that the knowledge of Blue Chip and its

[13] 328 US 293 (1946).
[14] Ibid, at 298-299.

actions should be attributed to each of the developers. It reached this conclusion by an extended application of the principles established by the Privy Council in *Meridian Global Funds Management Asia Ltd v Securities Commission*[15] for attribution of an employee's actions to a company in the statutory context of the New Zealand Securities Markets Act 1988, which emphasised the need to consider the policy of the legislation when approaching attribution. The Supreme Court found support for the same approach, in the context of conventional agency analysis, in its own decision in *Dollars & Sense Finance Ltd v Nathan*.[16] The conclusion reached on these findings was:

> *As such, the developers were parties to the actions of Blue Chip and its sales force with full attributed knowledge of the substance and detail of the Blue Chip products and that those products and the SPAs were marketed as integrated financial packages*.

On that basis the Court was satisfied that the sale and purchase agreements themselves did not fall within the exemption.

The judgment does not elaborate further on this finding, the result of which was that the obligations arising under the sale and purchase agreements were invalidated, along with the Blue Chip products themselves, under section 37(4) of the Securities Act. It is clear from the preceding analysis of the operation of section 37(4) on the sale and purchase agreements that the conclusion was again reached by viewing the transactions from the investors' perspective, whereby the Blue Chip products and the sale and purchase agreements were not separable. An investors' entry into the sale and purchase agreement was part of the subscription for the Blue Chip product, and so could not be enforced (and needed to be returned by the developers, given the finding that they also were issuers).

The lesson that can be taken from this conclusion is that just as *Culverden* revealed that some transactions should be unpacked to discover how the Securities Act applies to their component parts, so others must be viewed as a whole. Which approach should be taken in any case must again be decided from the investor's viewpoint. In *Culverden* the offer of the units to the intending residents clearly had its own purpose and value. In this case, as the Supreme Court observed, the purpose of the apartments to these investors was at best to provide some collateral to the financial promises made by Blue Chip. It was no part of the scheme designed by Blue Chip and presented to the investors that they should in fact end up with the apartments.

[15] [1995] 3 NZLR 7 (PC).
[16] *Dollars & Sense Finance Ltd v Nathan* [2008] NZSC 20, [2008] 2 NZLR 557.

Conclusion

Despite the reversal of almost every point decided in the Courts below, the Supreme Court's decision in *Hickman* can be seen as the result of a resolute application of two principles that Courts have held to apply to the Securities Act from its inception. First, the statutory language is deliberately broad, relying on statutory, regulatory, and administrative exemptions to temper any overreach. Secondly, analysis of transactions must be undertaken from the point of view of the investor. The Court's clear view in this case, to a greater degree than has been seen in securities litigation to date in New Zealand, was that analysis should also, with the purpose of the legislation in mind, focus on the substance rather than the form of the transaction. This implicitly departs from the approach of the Court of Appeal in *Society of Lloyd's & Oxford Members' Agency v Hyslop*:[17]

> *In each case it is crucial to keep in mind that the true character of a transaction can only be ascertained after careful consideration of the legal arrangement actually entered into and carried out and the forms adopted cannot be dismissed as mere machinery for effecting other purposes. Interrelated documents may be considered together but the legal rights and obligations of particular parties turn on the terms of their agreements.*

The twelve months since the delivery of the judgment have not seen any volume of products reclassified as "securities", despite the concerns expressed to the Court. The judgment has clarified the better approach to take to some classes of transaction previously seen as marginal. In some cases additional rigour in this approach has resulted in greater comfort that agreements thought to be "technical" securities, but where no investment purpose can be found, are not within the purview of the Act.

The direct effect of this decision on the application of the Securities Act may be limited by time, as a Bill before Parliament aims to repeal the Act over the next few years. However, as the replacement legislation, to be called the Financial Markets Conduct Act, unsurprisingly has a very similar investor-centred purpose to that of the legislation it replaces the case will have an enduring effect in terms of the approach to be taken when applying the new statute.

[17] [1993] 3 NZLR 135.