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AUSTRALIAN/NEW ZEALAND CASE LAW UPDATE — NEW ZEALAND

HON JUSTICE MARK O'REGAN
President, Court of Appeal of New Zealand[1]

[1] Thank you for the opportunity to address you. I am going to deal with a case on banking mandates and a case about the nature of "unclaimed money". It will not surprise you, given my historic connection with the PPSA in New Zealand, that I will then do a sort of pot-pourri of recent PPSA cases. I realise that, for Australian participants these will be jumping the gun somewhat, because your PPSA has not yet come into force, but I hope these cases will have some interest for you in illustrating the kinds of issues that the Australian PPSA will throw up. I will mention how the issues dealt with in the recent New Zealand cases would affect the equivalent sections in the Australian PPSA (with an appropriate disclaimer, given my lack of familiarity with the Australian PPSA). I will also mention a couple of recent securities law cases.

Banking

Westpac New Zealand Ltd v MAP & Associates Ltd: breach of mandate and dishonest assistance

[2] This case was an unsuccessful appeal by Westpac against a High Court decision finding that Westpac had breached its mandate with MAP and Associates Ltd, a small accounting firm in Hamilton.[2] MAP was appointed as deposit agent for funds to be paid to shareholders from the sale of a small, private Bolivian bank (Prodem) to a Venezuelan state-owned bank (Banco Industrial de Venezuela, CA (BIV)). It was to hold the purchase price in escrow until due diligence was carried out and the sale was finalised. Approximately US$50 million was credited by BIV to MAP's account with Westpac in

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1 I acknowledge with appreciation the contribution of my clerk, Amelia Keene, to the preparation of this paper.

2 *Westpac New Zealand Ltd v MAP & Associated Ltd* [2010] NZCA 404, [2011] 2 NZLR 90.

2006. BIV then assigned its rights to Bandes, another Venezuelan publicly owned bank. MAP advised that the funds should be disbursed in February 2008. Westpac became concerned due to a number of incongruities:

(a) It had originally been told it would hold the funds for a week;[3] in fact they were held for 21 months. Much of what it was told in 2007 about when it would settle proved unreliable.

(b) In February 2007, Westpac's Compliance Department had received a notice alerting the banking community to large payments being made from Bolivia and the need to treat them with caution.

(c) Westpac had been in touch directly with BIV and had received conflicting correspondence, including an indication that the sale had been cancelled.

(d) There were some difficulties establishing the details of the beneficiaries (account details were provided, but two names had been omitted).

(e) Westpac made some inquiries in February 2008 which led it to suspect or believe that the apparent principal of the consultancy firm charged with arranging the sale, a Mr Lara, was not in fact a director of that firm at the relevant time and neither was he a lawyer from a law firm based in Panama, as MAP had advised.[4]

(f) Some of the translations from the Spanish documents to English were inaccurate. In particular, the Spanish version of the escrow agreement did not seem to record Mr Anker as being the Seller's representative, whereas the English did.[5]

(g) The bank's original instructions were to pay the Bolivian shareholders. It was told a $600,000 fee would be paid to the consultants.[6] Its 2008

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3 At [54].
4 At [15].
5 At [58].
6 At [5].

instructions were to pay funds to persons not named as "sellers" in the escrow agreement. In fact, an affidavit filed later in the proceedings revealed that the consultants were to be paid $26 million from the funds.[7]

(h) Westpac received a letter in November 2007 which mentioned the assignment from BIV to Bandes, but the assignment was not specifically drawn to its attention. The Court found that it had at least been told of the assignment in a meeting on 31 January 2008.[8]

[3] Westpac did not disburse the funds as requested by MAP and instead suggested that MAP should apply to Court for orders for disbursement of the funds. The High Court ordered that it pay the funds.[9] It then issued a second judgment in which it found that Westpac had breached its mandate to MAP.[10] This second decision was upheld on appeal by the Court of Appeal. The Court discussed the scope of dishonest assistance and concluded on the facts that the circumstances were insufficient to justify Westpac's refusal to follow instructions on the basis that it would have been liable for dishonest assistance had it released the funds.

[4] There was some discussion of the scope of dishonest assistance. The Court held that the concept of a "reasonable banker" was helpful, following *US International Marketing Ltd v National Bank of New Zealand Ltd*.[11] The Court set out the law as follows:

> [46] Accordingly, we consider that a bank will be liable for dishonest assistance where it has actual knowledge of the circumstances of the transaction (the subjective element) such as to render its participation contrary to normally acceptable standards of honest conduct (the objective element). In assessing whether its participation is contrary to such standards, the concept of the reasonable banker may well prove helpful. In this context, factors such as the significance or unusual nature of the transaction, the customer's banking practices, banking practices within the relevant industry and statutory reporting requirements will be relevant.

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7 At [24].
8 At [14].
9 *MAP & Associates Ltd v Westpac Banking Corporation Ltd* HC Auckland CIV-2008-404-1373, 1 April 2008.
10 *MAP & Associates Ltd v Westpac Banking Corporation Ltd* (No 2) HC Auckland CIV-2008-404-1373, 10 March 2009 at [38]–[40].
11 At [46], *US International Marketing Ltd v National Bank of New Zealand Ltd* [2004] 1 NZLR 589 (CA) at [9] per Tipping J, at [78] per Glazebrook J.

> [47] Further, a bank may be liable even though it does not have actual knowledge of the circumstances of the transaction but has a well-grounded suspicion about them. In that situation the bank may be required to make further inquiry. A negligent failure to make inquiry will not establish liability. Rather, wilful blindness or a deliberate failure to make inquiry in order to avoid acquiring unwelcome knowledge is necessary.

[5] The Court found that Westpac should have disbursed the funds by 2 March 2008. By that time, it had received a letter from Mr Anker, who held a power of attorney for Prodem, confirming the beneficiaries and the transfer instructions. MAP had confirmed that Mr Anker held a power of attorney and Westpac had no grounds to doubt this. The Court found that Westpac's suspicions appeared to have been fuelled by a lack of familiarity with the practices and customs of those it was dealing with. It noted that it would have found expert evidence on international banking transactions such as these helpful. Ultimately, Westpac had to pay interest from the 2 March 2008 until the date of disbursement, at the rate set by the Judicature Act 1908. An award of indemnity costs made in the High Court was overturned.

[6] It might be said that this is a small price to pay in the face of potential liability if the funds were wrongfully disbursed. On the other hand, the consequences of wrongfully withholding funds can be much worse. In the *US International* case the appellant claimed that the failure to access funds had led to his being unable to complete a land purchase, meaning he forfeited his deposit of approximately $731,000 (the Court's decision was limited to liability and did not quantify the damages).

[7] The case has been welcomed by commentators for reiterating "the critical importance to commerce of banks honouring their mandates" and confirming the application of the "reasonable banker" test.[12] The lesson arising from the case has been described as "that [banks] should give precedence to their customer's interests and instructions and only ignore them in the most exceptional circumstances when the evidence that the funds belong to a third party is clear and established."[13]

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12 At [62]; Christopher Hare "Banking Law" [2011] 1 NZLR 121 at 156–157.

13 Hare, at 157.

[8] Whether this position is correct remains to be tested. The Supreme Court granted leave to appeal on the question of whether Westpac breached its mandate[14] and the appeal was heard on 31 May 2011. The decision has been reserved.

Westpac Banking Corporation v The Commissioner of Inland Revenue: unclaimed cheques and bank drafts

[9] The Unclaimed Money Act 1971 provides that unclaimed money should forfeit to the Crown. Unclaimed money includes:[15]

> Any other money, of any kind whatsoever, which has been owing by any holder for the period of 6 years immediately following the date on which the money has become payable by the holder.

[10] The question before the Supreme Court was whether unpresented bank cheques and bank drafts constitute unclaimed money for the purposes of the Unclaimed Money Act[16]. As Alan Tyree notes, an astonishing one percent of all bank cheques are not presented within six months of issue, so the sum at stake was potentially large.[17] If they are unclaimed money, the amounts must be paid to the Commissioner for Inland Revenue. If not, then, after six years, the bank will get a windfall. To fall under the definition of "unclaimed money", the money must have been owing for a period of six years. The question before the Supreme Court was whether, from the time of purchase of a bank cheque or bank draft, the money is "owing" and payable to the bank.

[11] I am sure it is unnecessary to explain bank drafts and bank cheques to an audience of banking and finance lawyers. Nevertheless, in the age of credit cards and internet transfers, a short definition, taken from the judgment, seems appropriate.[18] A bank draft is like a foreign currency cheque, which a New Zealand bank will issue. The payee (or its indorsee) named in the draft will then present it at a foreign bank, which will pay the amount denominated in a particular foreign currency. A bank cheque is a form of promissory note[19] whereby the drawer, a New Zealand bank, promises it will pay a

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14 *Westpac New Zealand Ltd v MAP & Associates Ltd* [2011] NZSC 1.
15 Unclaimed Money Act 1971, s 4(1)(e).
16 *Westpac Banking Corporation v Commissioner of Inland Revenue* [2011] NZSC 36, [2011] 2 NZLR 726.
17 Alan L Tyree "Unclaimed money" [2011] NZLJ 135.
18 At [3]–[4].
19 By section 84 of the Bills of Exchange Act 1908.

stipulated amount to the named payee (or its indorsee) on presentment of the draft. The named payee is usually not a customer of the New Zealand bank. A bank cheque is not a bill of exchange in terms of the Bills of Exchange Act 1908,[20] but a bank draft is.

[12] The case was an attempt by Westpac and other banks (the banks) to re-litigate a decision of the Privy Council in *Commissioner of Inland Revenue v Thomas Cook (New Zealand) Ltd*.[21] The Privy Council had decided the appellant company was liable to the Commissioner in respect of similar instruments to bank drafts, referred to as "international cheques". It held that to become payable, it was enough that the cheque had been issued. It was not necessary for it to be presented. As Lord Brown of Eaton-under-Heywood rather colourfully observed:[22]

> That surely would be the greatest nonsense of all: to say that money can only become unclaimed money once it has in fact been claimed.

[13] The Supreme Court reconsidered the point, but came to the same conclusion as the Privy Council. An amount may be payable (for the purposes of the Unclaimed Money Act) without actually being due (it becoming due on presentment).[23]

[14] In Australia, the equivalent unclaimed money legislation for "Authorised Deposit Taking Institutions" (ADIs) is s 69(1) of the Banking Act 1959. It provides:

> For the purposes of this section, unclaimed moneys means all principal, interest, dividends, bonuses, profits and sums of money legally payable by an ADI but in respect of which the time within which proceedings may be taken for the recovery thereof has expired, and includes moneys to the credit of an account that has not been operated on either by deposit or withdrawal for a period of not less than seven years.

[15] Unlike in the New Zealand context, the section contemplates that proceedings might be taken to recover the sum. For the amounts referred to in the first part of the section, they become unclaimed moneys once any causes of action have expired, for the balance of an account, they become unclaimed moneys once they have not been operated on for seven years.

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20 Bills of Exchange Act 1908, s 3(1).

21 *Commissioner of Inland Revenue v Thomas Cook (New Zealand) Ltd* [2005] UKPC 53, [2005] 2 NZLR 722.

22 At [16].

23 At [46].

[16] In a recent case note, Alan Tyree and John Sheahan concluded that Australia is trapped in the position considered to be "the greatest nonsense of all" by the Privy Council whereby money can only become unclaimed money once it has been claimed.[24] This is because in considering when the sums become "legally payable" for the purposes of s 69(1) of the Banking Act 1959 (Cth), s 58 of the Cheques Act 1986 (Cth) applies. This provides, in respect of bank drafts and bank cheques:

> ... a person who is the drawer or an indorser of a cheque is not liable on the cheque unless the cheque is duly presented for payment.

[17] The problem is that liability seems to rest on presentment. Whether Mr Tyree is right, and whether, if he is, Australian law mandates a nonsense, is something I leave in the capable hands of my judicial colleagues on this side of the Tasman.

PPSA

Tubbs v Ruby 2005 Ltd: the "ordinary course of business"

[18] *Tubbs v Ruby 2005 Ltd* involved the "ordinary course of business" test in the PPSA.[25] Mr Tubbs and Mr Gower were successful in the Court of Appeal on an appeal against a High Court decision declining to grant an injunction to freeze the proceeds of a sale by Ruby 2005 Ltd of timber it purchased from Waimate Timber Processing Ltd. Mr Tubbs and Mr Gower were receivers of Waimate, appointed by ANZ National Bank.

[19] The case was factually quite complex. Waimate and Ruby were closely related companies (Ruby's corporate shareholder has the same directors and shareholders as Waimate). They entered into an agreement whereby Ruby would buy timber from Waimate at market value when Waimate needed to achieve sales. The timber would then be Ruby's and would be stored separately by Waimate until a buyer could be found, at which time it would be sold and the profits accounted to Ruby. These transactions occurred frequently between 2005 and 2008. However in 2007, a fraudulent manager at Waimate sold Ruby's stock without authorisation and without properly accounting for it to Ruby. While insolvent, Waimate replenished the Ruby stock. Ruby then decided to sell

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[24] Alan Tyree and John Sheahan SC "Unclaimed Money: The Final (NZ) Word" (2011) 22 JBFLP 124 at 127.

[25] *Tubbs v Ruby 2005 Ltd* [2010] NZCA 353.

its stock to an overseas customer of Waimate, under its name. Soon after the sale, Waimate went into receivership. It is the proceeds of that sale that is now in issue.

[20] ANZ had a perfected security interest over Waimate's timber. It said that Ruby was effectively an unsecured creditor and therefore ANZ had priority. The Court rejected this argument. It said that Ruby was the owner of the timber under the agreement between Waimate and Ruby, and this trumped ANZ's interest.

[21] The Court also considered whether the transaction was carried out "in the ordinary course of business" under s 53 of the PPSA. The Court upheld the receivers' appeal that it was reasonably arguable that the transaction was outside the "ordinary course of business" and hence it would be appropriate to grant an interim injunction. It held that the timber sold by Waimate between 2005 and 2008 was within the ordinary course of business. That is, entering into an arrangement with a related party to ease financial pressure is within the ordinary course of business.[26] The key consideration was that the timber was sold at market price.

[22] However the Court was concerned about the 2009 transactions. It noted that there was a lack of evidence as to what knowledge Ruby had of its stockpile being depleted during 2009 (after the fraud by the manager had been discovered). If Ruby authorised the depletion, then it would simply become an unsecured creditor. When Waimate replenished Ruby's pile, it would have been replenishing it with Waimate's timber, over which ANZ had a perfected security interest. The Court held that these were arguably not sales and were outside the ordinary course of business either because they were in satisfaction of Waimate's existing debt; or because they were to account to Ruby for Waimate's conversion (through the fraud) of Ruby's stock. Accordingly, there was an arguable case the bank's interest survived the 2009 transaction and an injunction should be issued over the proceeds.

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[26] Compare: *Orix New Zealand Ltd v Milne* [2007] 3 NZLR 637 at [70], where Rodney Hansen J cites with approval Canadian jurisprudence suggesting that a private sale between two parties would not be within the meaning of "ordinary course of business": *Royal Bank of Canada v 216200 Alberta Ltd* (1986) 51 Sask R 146, at [22].

[23] In the decision under appeal,[27] the High Court judge had cited with approval the criteria from *Fairline Boats Ltd v Leger* for the "ordinary course of business" test:[28]

> (a) transaction type — the transaction should be one that is a normal part of the seller's business;
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> (b) place of sale — if made at the seller's business premises, it is more likely to be in the ordinary course of business;
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> (c) parties to the transaction — if the purchaser is an ordinary everyday consumer, the likelihood of a sale in the ordinary course of business is greater;
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> (d) quantity of the goods sold — if a large number of items are sold, many more than normally sold and forming a substantial portion of the seller's stock, this counts against it being a sale in the ordinary course;
>
> (e) price charged — if market price is charged, then the sale is more likely to be considered one in the ordinary course of business;
>
> (f) advertising — if the seller advertises, holding itself out to the public as conducting a certain business, the transaction is more likely to be in the ordinary course;
>
> (g) percentage of overall sales volumes.

[24] The Court of Appeal also cited *Fairline* but did not expressly endorse those criteria. *Fairline* is a case from Ontario, where the equivalent PPSA provision does not refer to the "ordinary course of business *of the seller*", but simply "the ordinary course of business". The Court of Appeal of Saskatchewan (where the wording is the same as in New Zealand) has suggested that caution is needed before applying Ontario cases.[29] It applies the test from the point of view of the seller: what is the ordinary course of business of the seller, whereas the Ontario approach is broader and looks to general commercial practice.[30] Nevertheless, the *Fairline* test is phrased in the context of the seller, and to some extent the differences between the approaches may be theoretical.

[25] In *Tubbs*, the decisive factor for the 2005–2008 transactions was the fact that Ruby had paid market value for the timber. For the 2009 transactions, the difficulty was that it

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27 *Tubbs v Ruby 2005 Ltd* High Court Timaru CIV 2009-476-615 26 February 2010 at [38].

28 *Fairline Boats Ltd v Leger* (1980) 1 PPSAC 218 (Ont HC); *Tubbs v Ruby 2005 Ltd* [2010] NZCA 353 at [22] and [38].

29 *Camco Inc v Olson Realty* (1979) Ltd (1986) 50 Sask R 161 (Sask CA).

30 *Agricultural Commodity Corp v Schaus Feedlots Inc* (2001) 2 PPSAC (3d) 270 (Ont SCJ); upheld on appeal: *Agricultural Commodity Corp v Schaus Feedlots Inc* (2003) 4 PPSAC (3d) 266 (Ont CA).

was not clear whether Ruby had agreed to lend the timber or not. If it had, the transactions were simply to dispose of a past debt, but in doing so ANZ's security was undermined. Because the case came to the Court as an appeal against an interlocutory application, the Court only had to decide that it was arguable that ANZ's security should have priority.

[26] The Australian PPSA adopts an "ordinary course of business" rule from the point of view of the seller as well. Section 46(1) provides that:

> **46 Taking personal property free of security interest in ordinary course of business**
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> Main rule
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> (1) A buyer or lessee of personal property takes the personal property free of a security interest given by the seller or lessor, or that arises under section 32 (proceeds—attachment), if the personal property was sold or leased in the ordinary course of the seller's or lessor's business of selling or leasing personal property of that kind.

[27] Accordingly, any New Zealand authorities are likely to be highly relevant.

Rabobank New Zealand Ltd v StockCo Ltd: "seriously misleading"

[28] *Rabobank New Zealand Ltd v StockCo* raised the issue of when a financing statement will be "seriously misleading" under the PPSA.[31] StockCo is a provider of lifestock financing. It retains ownership of the stock. The farmer in this case was a Mr Campbell. StockCo (or Mr Campbell acting as StockCo's agent) would purchase bulls (either from a third party or directly from Mr Campbell) and bail them to Mr Campbell. Mr Campbell paid interest on the purchase price to StockCo and would repay the purchase price once the stock was on-sold or slaughtered. Where the stock was purchased from a third party, this gives rise to a PMSI, which, if properly registered, takes priority over other security interests, such as that held by Rabobank. Where purchased direct from the farmer, no PMSI arises, since a purchase made under sale and leaseback arrangement is not a PMSI. Instead, Rabobank would agree to release certain stock from its general security, since the purchase money was being paid into a Rabobank account.

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[31] *Rabobank New Zealand v StockCo Ltd* HC Napier CIV-2009-441-207, 11 March 2011 per Simon France J.

[29] Rabobank raised a number of factual challenges to StockCo's security interest in the stock. However, for our purposes, the main legal issue was whether StockCo had a perfected PMSI over certain stock (those bulls purchased from a third party in 2007). StockCo had registered a financing statement. Rabobank challenged this statement as being seriously misleading under s 149 of the PPSA and therefore invalid. Section 150 goes on to state that a registration will be invalid if there is a seriously misleading defect in the name of the debtor stated.[32] The test is expressed as an objective one so it will not be necessary to prove that the defect actually misled the other party.

[30] There were a number of issues with the financing statement. First, it recorded Mr Campbell's name as "Alex Campbell" instead of the name as it appeared on his passport "Alexander Campbell".[33] The Court held that this was not sufficiently misleading to meet the standard in s 150. Second, Mr and Mrs Campbell had set up a partnership, but had not properly taken the steps to give effect to the partnership. No tax number had been obtained and it had never filed returns. For all intents and purposes, the farm operated as it always had, as the sole business of Mr Campbell. The financing statement was signed by both Mr and Mrs Campbell and the debtor recorded as an organisation as "AM and MJ Campbell". Rabobank challenged this as misleading. It said that the partnership's trading name of "Awapapa Station" ought to have been used (as recorded in the partnership deed).

[31] As Eady and Jackson noted in a 2006 Law Society paper, the Courts could have adopted two approaches to the test:[34]

> ... the test applied could be whether a person searching the PPSR and taking all prudent steps to ascertain whether there were any financing statements registered in respect of particular collateral would realise that the particular financing statement did relate to that collateral. Such a test may require searchers to use wildcard searching functions and the like. At the other end of the scale, the courts may take a strict approach that any error in a field which could be searched on will make a financing statement seriously misleading.

[32] The Judge adopted the broader, more purposive approach. He found that the partnership deed had never been brought into effect and the trading name of Awapapa

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32 The same provisions are included in the Australian PPSA: s 164 provides the registration will be invalid if there is a "seriously misleading defect" in any data.

33 Personal Property Securities Regulations 1999, schedule 1, cl 2(2).

34 Peter Eady and Adam Jackson "PPSA – a review four years on" (paper presented to New Zealand Law Society Seminar, October 2006) at 36.

Station was not used. Indeed, Rabobank had conceded that AM and MJ Campbell was a trading name used by the Campbells. The Judge accepted the evidence that anyone searching on the register would have searched by name and by any trading name, and would have found the financing statement. There was no risk that third parties would have been misled by the failure to refer to trading name in the partnership agreement of Awapapa Station.[35]

[33] The case illustrates the difficulties that can arise in accurately recording the debtor details. Technically, the legal owners are the partners, which suggests that the two names of the individuals should be noted. On the other hand, a partnership is an organisation and must be registered as such.[36] Clause 6 of the Regulations recognises this difficulty, stating that if the name of the organisation is not set out in the constitution then the trading name it is commonly known by will suffice. In the Campbells' case, it was not clear which rule should apply. Most mail and invoices was addressed to Mr Campbell, some to the partnership and some to Mr and Mrs Campbell as individuals. The partnership deed gave the trading name as Awapapa Station but the Judge found the parties had not given effect to this. In this factual context, the Judge's purposive approach seems appropriate, but does highlight the difficulty that can arise simply in recording a name correctly.

[34] The Judge said he would have taken a similarly robust approach to Rabobank's financing statements (which were challenged by StockCo: it was unnecessary to decide the point because StockCo succeeded in establishing that it had a perfected PMSI). Rabobank had not been particularly diligent in accurately recording the stock released from its general security. The Judge described its approach as "haphazard".[37] At times the stock numbers were significantly understated. This was quite different to *Simpson v New Zealand Associated Refrigerated Food Distributors Ltd*, where a secured party overstating its security interest was found not to be misleading since a searcher could have inquired and ascertained the correct position.[38] Nevertheless, the Judge tentatively held that anyone checking the security would have realised that stock numbers fluctuate and would have

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35 At [77].
36 Personal Property Securities Regulations 1999, schedule 1, cl 6 and 7.
37 At [86].
38 *Simpson v New Zealand Associated Refrigerated Food Distributors Ltd* [2007] 2 NZLR 130 (CA).

been on notice that there was a general security interest and made further inquiries.[39] Accordingly the error was not considered to be significant. This accorded with the broad purpose of the financing statement. It was intended only to notify a third party in generic terms of a possible security interest in the debtor's property. If a third party required further information in regards to certain collateral, then they could use the procedure set out in s 177(1)(c) of the PPSA.[40]

[35] Rabobank had used the trading name "Awapapa Station" and Stockco challenged this as seriously misleading. The Judge did not decide the point as the facts were unclear about the name used by the Campbells at the relevant time. But he said if the correct trading name was Mr Campbell's or A J and M J Campbell, the registration would have been seriously misleading.

Rabobank New Zealand Ltd v McAnulty: bailments

[36] *Rabobank New Zealand Ltd v McAnulty* raised a tricky issue on the correct interpretation of the definition in the PPSA of a "lease for a term of more than 1 year".[41] The case involved a thoroughbred stallion owned by a Syndicate that had decided to put the horse out to stud. It bailed the horse with a stud farm. The stud farm then went into receivership and the question was whether Rabobank, which held a perfected interest over all of the farm's property, had priority in the stallion.

[37] Under the PPSA, a lease is deemed to be a security interest if it is a "lease for a term of more than 1 year."[42] Such a lease is defined to include a "lease or bailment".[43] There were two issues before the Court of Appeal. The first was whether the arrangement fell within the definition of a "lease for a term of more than 1 year". The second was whether the exclusion to that definition applied: that the bailor was not in the business of leasing.[44]

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39 At [94].
40 Compare Personal Property Securities Act 2010 (Cth), ss 274–283.
41 *Rabobank New Zealand Ltd v McAnulty* [2011] NZCA 212.
42 Personal Property Securities Act 1999 (NZ), s 17(1)(b).
43 Personal Property Securities Act 1999 (NZ), s 16(1)(a).
44 Personal Property Securities Act 1999 (NZ), s 16(1)(c)(i).

[38] The arrangement with the stud farm was nothing like a lease. The stud farm cared for the horse and organised its nominations, and in return received a fee and a share of the nominations. The bailor paid the bailee, rather than the bailee paying rent to the bailor. The Court decided that the agreement was a lease for a term of more than one year but found that the business exclusion in s 16(1)(c)(i) applied: that the arrangement was a "lease by a lessor who is not regularly engaged in the business of leasing." To achieve this result, the Court had to read the word "lease" in (c) as a shorthand for "lease or bailment" as used in paragraph (a), which it justified on the basis of the presumption against absurdities in legislation.

[39] The Court rejected the Canadian jurisprudence on the meaning of "regularly engaged in business", which suggested a single transaction could constitute regular engagement in the business of leasing if it was a "proper component" of the business.[45] Instead, the Court applied a commonsense interpretation of the phrase that would exclude bailments where the bailor was not intending to profit from the lease.[46] It was unlikely that a syndicate that had merely entered into one arrangement was "regularly" bailing. Here, the bailor was paying the bailee to care for the horse. The bailment was excluded from the scope of s 16(1)(a) and since it agreed that it was not otherwise a security interest for the purposes of s 17, the PPSA did not apply.

[40] The Australian PPSA is much clearer than the New Zealand PPSA on this issue. It adopts the term "PPS lease" to include a lease or bailment.[47] Under s 12, the interests of a lessor or bailor of a PPS lease is deemed to be a security interest whether or not it "in substance" secures payment or performance of an interest. The Australian courts will not have to rely on the word lease to convey the concept of bailment as well. Section 13(2)(a) provides an express exception where the bailor is not regularly engaged in the business of leasing goods. Further, s 13(3) provides that the definition applies only to bailments where the bailee provides value. It is likely that this section was intended to exclude bailments where the bailee does not pay rent, although it might be argued that the word "value"

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45 *Rabobank* at [46]–[48]; See *David Morris Fine Cars Ltd v North Sky Trading Inc* (1994) 8 PPSAC (2d) 112 (ABAQ); aff'd *David Morris Fine Cars Ltd v North Sky Trading Inc* [1996] 7 WWR 332 (ABCA); *Paccar Financial Services Ltd v Sinco Trucking Ltd* (1987) 7 PPSAC 176 (SKQB) and *Karkoulas v Farm Credit Canada* (2005) 8 PPSAC (3d) 249, additional reasons at (2005) 9 PPSAC (3d) 142 (SKQB).

46 *Rabobank* at [40]–[41].

47 Personal Property Securities Act 2009 (Cth), ss 10 and 13.

includes a bailee who provides non-cash consideration. Section 10 defines "value" as "consideration that is sufficient to support a contract", which might mean that only purely gratuitous bailments are excluded by s 13(3). This could be used to justify departing from *Rabobank*, in that there seems to be a statutory indication that where consideration is paid by the lessee it will constitute a PPS lease. Further, the inclusion of the separate category of "bailments" at all might suggest that something other than a lease arrangement was intended to be caught.[48]

[41] The Australian courts may look to New Zealand's jurisprudence in interpreting the business exception to require that the bailor is actually intending to make a profit from the bailments and that there must be more than one such arrangement intended for it to be "regularly engaged" in this business. It is unfortunate that the Canadian and New Zealand courts appear to have parted ways in this respect, and, until a case is decided, it will not be clear what approach the Australian courts will adopt.

[42] For Australian practitioners seeking to get to grips with the effect of the Australian PPSA, the *Rabobank* decision highlights the importance of considering the PPSA implications of any lease or bailment agreement entered into and being aware of the deeming provisions of the PPSA. The Syndicate in *Rabobank* gave evidence that:

> The February Syndicate did not at the time nor has it ever owed any money to [the Stud Farm] or to Rabobank. ... Words like "security" never entered the discussions between [the Stud Farm] and the February Syndicate. We didn't even know that there was something called the Personal Properties Securities Act.

[43] The Syndicate were lucky that the business exception applied and they could avoid the effect of the PPSA. If it had not applied, they would have lost a million dollar horse for a failure to register a financing statement.

[44] In the event of bankruptcy, winding up or administration, the position of a holder of an unperfected interest is even starker under the Australian PPSA. Whereas the failure to perfect in New Zealand means the security is subordinated to perfected security interests,

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[48] Note, however, that paragraph (c) of the definition of "grantor" in s 10 of the Australian PPSA refers to "a lessee under a PPS lease", rather than "a lessee or bailee under a PPS Lease". Contrast this with s 13 where the phrase "lessee or bailee" is used.

my understanding is that in Australia it will effectively relegate the security holder to being an unsecured creditor.

The Healy Holmberg Trading Partnership v Grant: priority by perfection?

[45] This case concerned the PPSA priority rules. The case involved the Healy Holmberg Trading Partnership (Healy) which agreed to make loans to LBD Civil Ltd (LBD), which LBD used to buy vehicles and equipment. On 29 January 2006, Healy registered a financing statement on the PPSR. Another creditor, RIGA Investments Ltd (RIGA) loaned LBD money and registered a financing statement on the PPSR on 9 August 2007. LBD was placed into voluntary liquidation on 17 April 2008. The liquidators asked for copies of Healy's security agreements. There was some delay before these were provided. The liquidators became suspicious and engaged a documents expert who deposed that the agreements had most probably been executed as a stack on 31 August 2007 and had been backdated (some to as early as 2005). The Court accepted that the agreements were signed, at the earliest, on 31 August 2007. The issue then was whether Healy had priority.

[46] The High Court held that "the greatest priority is given to a security interest holder who perfects first".[49] Since Healy had not executed security agreements before RIGA registered (it not being contested that RIGA had perfected its interest), RIGA had priority:[50]

> HH cannot claim that its time of registration is the time of priority pursuant to s 66 given its failure to comply with s 36 and the fact that, at the time of registration, there was no security agreement, oral or otherwise capable of being perfected. Therefore perfection pursuant to s 41 could only occur upon attachment pursuant to s 40, being the time that security agreement was reduced to writing as per s 36.

[47] Professor Gedye has suggested that, even accepting the factual findings, the views expressed by the Associate Judge on priority by perfection are incorrect.[51] He says that priority is not governed by perfection, but, most commonly, by registration under the residual priority rule in s 66(b)(i) of the PPSA. He says that if priority is determined by a first to perfect rule, then it undermines the purpose of the PPSA to provide clear and

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49 At [33].
50 At [66].
51 Mike Gedye "First to perfect?" [2011] NZLJ 123.

certain priority rules where the priority of creditors can be ascertained from a search of a centralised securities register.

[48] The priority provisions in the Australian PPSA follow substantially the same regime as that followed in the New Zealand and Canadian PPSAs. Under s 19(1)(b)(iii) of the Australian PPSA, the security interest is enforceable against third parties only if in writing.[52] But there is greater flexibility in the Australian provision for an act or omission to be used to confirm a term where the grantor has not signed the written agreement. The residual priority rules in s 66 of the New Zealand PPSA are reflected in s 55 of the Australian PPSA and are substantially the same.

Marac Finance Ltd v Greer: PPSA and the Land Register

[49] Another PPSA case that merits a brief mention is a High Court decision *Marac Finance Ltd v Greer*.[53] The case involved a mortgagee (Equitable) with a mortgage registered under the register set up by the Land Transfer Act 1952 and a financier (Marac) that had registered a general security interest over all present and after-acquired property of the debtor. Equitable had received all the rent paid since the debtor had gone into receivership. Marac sued saying it had priority and was thus entitled to the rent. The question was thus whether the first-ranking mortgagee trumped the first-ranking security interest under the PPSA. The Judge focused on s 23(e) of the PPSA, which provides:

> (e) An interest created or provided for by any of the following transactions:
>
> (i) The creation or transfer of an interest in land:
>
> (ii) A transfer of a right to payment that arises in connection with an interest in land, including a transfer of rental payments payable under a lease of or licence to occupy land, unless the right to payment is evidenced by an investment security:

[50] He concluded that s 23(e)(ii) excludes rent paid from the scope of the PPSA because rent is a right to payment that arises in connect with an interest in land.[54] This

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52 Mirrors s 36 of the Personal Property Securities Act 1999 (NZ).

53 *Marac Finance Ltd v Greer* HC Auckland CIV-2010-404-4957, 17 March 2011.

54 At [38].

leaves priority in rental payments to be decided under the Land Transfer Register in the same way as would occur in any other contest as to priority between mortgages.[55]

[51] There is a similar provision in the Australian PPSA. Section 8(1)(f)(ii) of the Australian PPSA provides that the Act does not apply to "the creation of an interest in a right to payment, or the creation or transfer ... of a right to payment, in connection with an interest in land, if the writing evidencing the creation or transfer specifically identifies that land".

Toll Logistics (NZ) Ltd v McKay: common law liens under the PPSA

[52] Section 93 of the PPSA gives a super-priority to any common law lien. It provides:

> **93 Lien has priority over … security interest relating to same goods**
>
> A lien arising out of materials or services provided in respect of goods that are subject to a security interest in the same goods has priority over that security interest if—
>
> (a) The materials or services relating to the lien were provided in the ordinary course of business; and
>
> (b) The lien has not arisen under an Act that provides that the lien does not have the priority; and
>
> (c) The person who provided the materials or services did not, at the time the person provided those materials or services, know that the security agreement relating to the security interest contained a provision prohibiting the creation of a lien by the debtor.

[53] Subject to a number of conditions, the holder of a lien has priority over the holder of a perfected security interest.[56] The example given in the PPSA is where person A has a perfected interest in person B's car. B then takes it to person C, a mechanic, for repairs. If person C holds a common law lien over the car, that will trump person A's perfected interest.

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55 At [40].

56 Section 66 provides that a perfected security interest has priority over an unperfected security interest, and that first to register has priority, but it is a default rule. So a perfected security interest will be trumped by any other interest that is given priority by the Act, including a common law lien under s 93.

[54] In *Toll Logistics*, the issue was whether there was a common law lien that would give Toll priority before ASB, which held a perfected security interest.[57] Toll was a warehouse operator and provided a number of logistical services to Scene 1 Entertainment Ltd (Scene 1), including breaking down pallets, re-packaging and transporting. Toll held approximately 500,000 of Scene 1's DVDs, worth approximately $2.6 million, when Scene 1 was put into receivership. ASB was owed about $7 million and sought to recover some of this sum by selling the DVDs. Toll was owed about $280,000 and claimed that it had priority as it had a general packer's lien. The Court found that New Zealand courts have not recognised a packer's lien without proof of custom to support it, and that Toll had not so proved.[58] In so finding, the Court took its cue from a High Court of Australia case: *Majeau Carrying Co Pty Ltd v Coastal Rutile Ltd*, where the majority held that no general warehouseman lien arose in common law and that the evidence that it was custom in the Brisbane area did not support its existence.[59] This suggests that the Australian courts would also adopt an approach whereby Toll would not have priority under the PPSA.

[55] The Court also noted that to the extent Toll had entered into a contractual lien this displaces any common law lien, and would have meant that Toll did not have priority in any case. This is because only "liens... created by any other Act ... or by operation of law" are excluded from the scope of the PPSA.[60] Although the language of s 93 refers to "lien" this has to be read subject to s 23.

[56] The case is primarily interesting for the discussion of common law liens. From a PPSA perspective, it is one of only a few cases concerning s 93 and may be helpful to future courts seeking to interpret the section:[61]

> Section 93 of the PPSA may be viewed as a limited exception to the broad intention to codify the law of security interests in personal property. While the existence of common law liens was accepted by s 93 as an exception to this general intention, anything other than a cautious approach to the recognition of common law liens is not justified.

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57 *Toll Logistics (NZ) Ltd v McKay* [2011] NZCA 188, [2011] 2 NZLR 601.
58 At [55].
59 *Majeau Carrying Co Pty Ltd v Coastal Rutile Ltd* (1973) 129 CLR 48.
60 Section 23(b).
61 At [60].

[57] The High Court has subsequently found a common law lien in at least one case. In *StockCo Ltd v Walker*, the Court found that StockCo's perfected security interest in stock was trumped by a common law lien held by Ms Walker, a third party who was grazing the stock.[62] The Court placed importance on the fact that the grazing contract expressly linked payment with her fattening the bulls up. It was not merely a contract of agistment, but one of improvement. The contract did not mention liens. Since Ms Walker had possession of the stock, she had a common law lien and was entitled to retain possession until payment of the money owed to her under the grazing contract.

[58] *Toll Logistics* is relevant in Australia since the applicable provisions of the Australian PPSA are substantially the same.[63]

Securities

Hickman v Turn and Wave Ltd: the meaning of "debt securities"

[59] This case[64] concerned the "Blue Chip" a property investment scheme that was also the subject of the Bartle litigation dealt with at another session of this conference.[65] The appeal concerned a certain scheme promoted by the Blue Chip group. The scheme sought investors who signed agreements to purchase apartments in Auckland as part of their investments with Blue Chip. The developers of the apartments were found to be independent of the scheme. The investors signed the sale and purchase agreements directly with the developers and signed an investment agreement with Blue Chip. The purchase was subject to a deed of nomination whereby Blue Chip undertook to lease out the apartments on behalf of the investor, with payment of the rent guaranteed by Blue Chip. The relevant Blue Chip companies collapsed. The developers then called on the investors to settle.

[60] The appeal raised a number of issues, but I will focus on the securities issues. The investors argued that both the investment agreements and the sale and purchase

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62 *StockCo Ltd v Walker* HC Napier CIV-2011-441-110, 24 June 2011.

63 See ss 8, 73 and 140.

64 *Hickman v Turn and Wave Ltd* [2011] NZCA 100.

65 *Bartle* was another case resulting from the collapse of the Blue Chip group: *Bartle v GE Custodians Ltd* [2010] NZCA 174, [2010] 3 NZLR 601; overturned on appeal: *GE Custodians Ltd v Bartle* [2010] NZSC 146, [2011] 2 NZLR 31. I do not discuss it in this paper because it is the subject of another session at this conference.

agreements were void as the investment agreements constituted "debt securities"[66] under the Securities Act 1978. Since (as was common ground) there was no registered prospectus relating to the scheme, the offer and allotment of securities to the public would contravene the Securities Act and would be void.[67] To succeed, the investors also had to show that the Blue Chip investment agreements were not exempted from the Securities Act[68] and that the sale and purchase agreements could not be severed from the Blue Chip investment agreements and/or were tainted by their illegality and therefore void and of no effect.

[61] The offer of the Blue Chip scheme to the public could contravene the Securities Act only if the offer amounted to an offer of securities. Section 2D(1) defines security as "any interest or right to participate in any capital, assets, earnings, royalties, or other property of any person; and includes– ... (b) a debt security". Section 2 defines "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". The definition sets out a number of examples that are said to be included within the concept of debt security, such as debentures, bonds, notes, certificates of deposit and convertible notes. The Court found that "debt security" should be interpreted to cover situations where there is a repayment obligation on the offeror and that the "otherwise owing" reference had to be read as taking meaning from the preceding words, "deposited with" and "lent to". The examples included within the definition reinforced this. None of the agreements entered into with Blue Chip placed a binding obligation on Blue Chip to repay the amount paid by the investor. This factor was determinative in the Court's reasoning to conclude that they were not debt securities.

[62] The Court relied on a Privy Council decision in respect of New Zealand, *Culverden Retirement Village v Registrar of Companies*.[69] A retirement village offered to the public opportunities to purchase units in the village. It was a term of the sale and purchase agreement that upon ceasing to live in the unit, the village would buy it back at a set price. The transaction amounted to a debt security whereby the owner of the retirement village

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66 As defined by the Securities Act 1978 (NZ), s 2.
67 Securities Act 1978 (NZ) ss 33(1) and 37(4).
68 Section 5(1)(b).
69 *Culverden Retirement Village v Registrar of Companies* (1996) 1 BCSLR 162 (CA) at 166; [1997] 2 NZLR 257 (PC) at 261.

issued the occupier a right to be paid money on the eventual re-transfer of the unit.[70] The exemption in s 5(1)(b) for real estate did not apply since the buy-back condition was a "cardinal feature" of the transaction.[71]

[63] The Court went on to consider whether, if there had been debt securities, the agreements would be exempted under s 5(1)(b) as agreements "in respect of... any estate or interest in land". It held that it would not have been open to the issuer to rely on the exemption in respect of the agreements, following *Culverden*.[72] Any money due, as under the buy-back option, such as repayment of the deposits and payment of reasonable settlement costs, would not be exempted as they were unusual and important parts of the arrangement. However the leases would have been exempted, since they are not unusual and clearly related to land.

[64] Even if the appellants had succeeded in persuading the Court that some aspects of the Blue Chip scheme fell within the definition of "security" and that the exemptions in the Securities Act did not apply, they would still have needed to show that the sale agreements under which the investors bought the apartments were tainted by the illegality (non-compliant offers of securities). The Court upheld the High Court finding that there was no tainting. There was no evidence to show the sale agreements had as their purpose the promotion of the agreements said to contain the non-compliant offers of securities and the apartment developers (and sellers of the apartments) did not have actual or constructive knowledge of those agreements.

[65] Investors have applied for leave to appeal to the Supreme Court on the issues relating to the definitions of "security" and "debt security".

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70 The Securities Act has since been amended so that security interests in retirement villages are covered, see s 107(2) of the Retirement Villages Act 2003 and s 5(1)(b)(k) of the Securities Act.

71 At 260.

72 At [342], [349] and [351].

R v Steigrad: criminal liability under s 58 of the Securities Act

[66] *R v Steigrad* involved a challenge to the particulars of an indictment for one of five directors charged with breaches of the Securities Act following the collapse of one of New Zealand's finance companies, Bridgecorp Ltd, in 2007.[73]

[67] Mr Steigrad submitted that he had been wrongly charged under s 58 for prospectuses and investment statements that were accurate when first distributed and merely became untrue because of an intervening change of circumstance. The High Court accepted that distribution occurred once: at the initial act of making the document available. This was overturned by the Court of Appeal, which held that distribution may be continual and occur through the many different ways the information is available to the public. Each of these distributions may technically constitute a breach of s 58. Therefore information included in the prospectus and investment statement that subsequently became untrue did give rise to criminal liability under s 58. One strong factor supporting the Court's decision was the change in the wording of the legislation from the original "issued" to "distributed", suggesting a broader meaning was to be attached to "distributed" that would include continuing availability of the documents.[74]

[68] The Court recognised that its decision could be criticised by practitioners questioning the practicalities of refreshing an investment statement and prospectus each time the financial situation changes. To take one example from Mr Steigrad's case, one of the charges related to a claim in the prospectus that said Bridgecorp had never missed an interest payment or repayment of principal when due. Three months after its registration, this statement was no longer true. The decision places a positive obligation on directors (and their advisors) to continue monitoring the accuracy of the statements and prospectuses, particularly where the financial viability of the company takes a turn for the worse. The Court said:[75]

> Concerns about compliance costs on promoters and directors cannot be allowed to neuter what this Court has held to be the "broad statutory goal" of the

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73 *R v Steigrad* [2011] NZCA 304; on appeal from decision of High Court: *R v Petricevic* HC Auckland CRI-2008-004-29179, 25 March 2011.

74 At [98].

75 At [114].

> S[ecurities]Act: facilitating "the raising of capital by securing the timely disclosure of relevant information to prospective subscribers for securities".

[69] But the Court also suggested that the defence of reasonable belief might be extremely important in this context, since only "reasonable" monitoring of the ongoing accuracy of statements would be required.[76] Careful consideration of what is reasonable on the facts of each case will be required. Moreover, the no fault defence should ensure that directors are not held responsible for breaches of the Securities Act that occur after they have resigned, but relating to statements they authorised that were correct at the time.

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[76] Testing of the scope of this defence has already generated a number of interesting cases in the New Zealand context, the most recent of which being the successful prosecution of the directors of failed finance firm Nathans Finance Ltd: *R v Moses* HC Auckland CRI-2009-004-1388, 8 July 2011.