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Justice back to the community

The guest editorial for this month is the speech made by Chief District Court Judge Trapski at the opening of the Porirua District Court on Wednesday 12 August 1987.

Mayor, Honourable Minister, Your Honours, Rangatira, all distinguished guests on this *paepae*, Ladies and Gentlemen: It is a great pleasure to be here with you for the opening of this Porirua District Court and Probation Office for this is a very clear manifestation of the policy of being seen to take justice back to the community so that the community can be represented fairly and squarely with its very own problem of dealing with, reforming and above all rehabilitating its own misfits.

Throughout most countries of this world people are, and have for centuries been concerned with the rate of crime in their communities and of its effect. It is clear that the more civilised the community, the more concerned it becomes about its crime rate and about the effect of that crime on its citizens.

A wealth of experience, research and study over centuries, but more particularly in this the 20th century, has clearly and consistently shown that the problem of crime, except violent offending of a serious kind, is not solved in prisons, no matter how austere or spartan they may be, but that criminals can be reformed and their actions can be ameliorated by their absorption into a loving, caring and supportive community.

There is, of course, nothing new in this philosophy: It was advocated so eloquently by a man called Jesus Christ some two thousand years ago, and it is his philosophies which we are told form the basis of our way of life in this country today.

But it is also the philosophy which has been espoused by most, if not every worthwhile philosopher and thinker who has ever walked this planet, down through the centuries: And it must be true today.

But of course there will be failures, because in attempting to solve crime we are attempting to modify human behaviour and we are told, quite simply and quite clearly, that is a never-ending task and a ceaseless quest for man.

So it is that here in Porirua, by the commissioning of this Courthouse and Probation Office, we are making our attempt to ameliorate the insoluble, by bringing to the midst of the community the opportunity for it to respond to the call to do something about crime and its effects; to work on the perpetrators of that crime; to change their ways by encouraging them into the opportunity of living in a loving, caring and supportive community, so that their dignity and their self-esteem can be cultivated to the extent that they become part of that community, with the growing desire to contribute to it, rather than to destroy it and its members.

Porirua, like West Auckland and South Auckland, has its problems: but like those communities, it also has an abundance of support systems and a depth of community spirit. It is now that this spirit and those support systems can and will be tapped to maximum advantage in a way that is positive, tailormade, and unique to Porirua.

The Judges who will service the Porirua district in this Courthouse have already dedicated themselves, strident criticism notwithstanding, to that Christian and well-tested goal.

To that end Judge Carruthers who is one of the Judges committed to that goal, was here with you at dawn this morning to lift that tapu on this site.

For my part, it is my privilege to sincerely and publicly wish all who come to serve their fellow man within the confines of this building, continued resolve in their work and much success.

Arohanui.Kia ora tatou.

P Trapski
Chief District Court Judge

Case and Comment

The Court of Appeal and recklessness

In *R v Harney* [1987] BCL 1343 the Court of Appeal reconsidered the meaning of s 167(b) Crimes Act 1961 which provides that a killing is murder where the accused deliberately inflicted bodily injury knowing such injury to be likely to cause death, and being reckless as to whether that death ensues. The decision is of importance to criminal lawyers on two counts: (1) it settles the meaning (or lack thereof) of reckless in s 167(b); and (2) much more importantly, the Court makes some obiter observations concerning the meaning to be given generally to the troublesome concept of recklessness in New Zealand criminal law.

A *The Trial*

Harney (18) was charged with the murder by stabbing of an English soccer player during a street brawl one Saturday night in Napier. The defence was conducted on two separate fronts – lack of murderous intent (it was argued that Harney aimed at a leg rather than the ultimate venue of the stomach) and provocation (the accused's girlfriend had been struck by the deceased prior to the killing). Both defences were rejected by the jury which apparently based its verdict on the s 167(b) limb of murder.

The appeal was argued in relation to the lack of murderous intent. The trial Judge had instructed the jury that the accused must (1) have the specific intent to inflict bodily injury which he knew was likely to cause death, and (2) be reckless as to that result, reckless being defined in these terms:

> Recklessness is present when someone does an act which creates an obvious risk for the safety of another, and when he does that act he *either has not given any thought to the possibility of there being any risk*, or has recognised some risk involved and has nonetheless gone on to do it (my emphasis).

The objection taken to this direction related to the emphasised part, which it was said wrongly introduced an objective element into what should be a wholly subjective test. The Court of Appeal accepted this argument. However it ruled that, given the tenor of the whole instruction, the error was immaterial. The conviction was therefore affirmed.

B *Section 167(b) Crimes Act 1961*

This is at least the fourth time that the Court of Appeal has been called upon in recent times to consider the meaning to be given to ss 167(b) and (d) Crimes Act 1961. (See also *Dixon* [1979] 1 NZLR 641, *Gush* unreported, CA 220/79; *McKeown* [1984] 1 NZLR 630, and *Piri* unreported, CA 126/86.) Two main problems emerge with subsection (b). The first (not in issue in this case) is the meaning to be attributed to "likely to cause death"; the second is the content to be given to the concept of recklessness.

Concerning the first, it may assist with understanding the trial Judge's error to recall the meaning the Court of Appeal had previously given to "likely". After the lengthy discussion in *Piri* (supra), the Court accepted that the word did not require the accused to have indulged in a fine assessment of the percentages and to have arrived at a "more likely than not" conclusion. Rather, in the words of McMullin J (p 5), "likely" refers to "a death of which there is a real and substantial risk". With this definition incorporated into the section, the jury in *Harney* were instructed that what occurred would be murder if

> the offender meant to cause any bodily injury which *was known to the offender* to involve a real and substantial chance of death and when doing that act *the offender had not given any thought* to such a possibility.

Clearly this is a nonsense. One cannot realise something is possible and at the same time have not given any thought to it. However the purpose of this note is not to condemn an error made in the context of a complex jury instruction. Rather it is submitted that two outside factors can be seen to have had a direct link to the mistake made. The first is the drafting of the section, the second the Court of Appeal's own judgment in *Howe* [1982] 1 NZLR 619.

Concerning the drafting, the Court of Appeal had previously (*Dixon*, supra) cast doubt on whether recklessness added anything to the balance of the section. Now in *Harney* the Court has confirmed that the final limb of s 167(b) is indeed otiose. If "reckless" were to be given a meaning it would be in terms of its traditional subjective definition, and would therefore require a defendant to have been aware that death might result. Given that the first part of s 167(b) specifically requires knowledge of the possibility of death, recklessness clearly adds nothing. The trial Judge's error, then, was in trying to define the word at all. In the context of this section the better approach is to advise the jury, as indeed the trial Judge did at a later stage, that if the jury was satisfied that the accused knew death was a real chance "then the recklessness element really follows". It is to be hoped that the drafters of the new Crimes Bill save much heartache by simply omitting the offending words.

C *Recklessness in general*

Despite frequent assertions in certain sectors of despair and

anarchy, the homicide rate in New Zealand is not yet such that all criminal lawyers need to be totally familiar with the workings of the murder provisions. Accordingly, it is likely that *Harney* will be of greater significance for the Court's observations on the meaning to be given generally to recklessness in the criminal law.

The recent history of recklessness has been a chequered one, particularly in England where the efforts of Lord Diplock have reduced the concept to little more than negligence restated. In New Zealand, the Court of Appeal in *Howe*, in a judgment surprisingly and disappointingly lacking in any supporting argument on this point, adopted the new *Caldwell* or objective recklessness for s 90 Crimes Act 1961 (now repealed). Since *Howe* several High Court judgments have adopted the objective definition. (Barker J lists several in his judgment in *Jefferson v Ministry of Agriculture and Fisheries*, unreported, M 286/85 Rotorua Registry.) It is submitted that it was probably *Howe* which prompted the trial Judge in *Harney* to define the term in an objective sense. In *Howe* the Court of Appeal made it clear that it was not laying down that recklessness should always be objective. Sometimes it would mean one thing, other times another. Unfortunately, the Court never explained how one was to decide which it was to be, and in *Harney* the trial Judge simply backed the wrong horse.

Now, the Court of Appeal has revisited *Howe*; it has maintained its stance that both types of recklessness have a place in New Zealand, but has now asserted that (p 7):

> we incline to the view that recklessly has usually been understood in New Zealand to have the meaning given in pre-*Caldwell* textbooks such as 11 *Halsbury's Laws of England*, 4th edition, para 14, and *Adams on Criminal Law in New Zealand*, 2nd edition, para 1430. That is to say, foresight of dangerous consequences that could well happen, together with an intention to continue the course of conduct regardless of the risk

At the least a presumption is created. Normally recklessness will have its pre-*Caldwell* subjective meaning. Again though when the exceptions will be we are not told. As an intractable opponent of the new recklessness, I welcome any move to limit its presence in New Zealand. However, just as opponents of *Caldwell* recklessness could feel aggrieved at the lack of argument which heralded its introduction into New Zealand in *Howe*, so it must be that proponents of it (and there are some), will feel aggrieved at this latest retrenchment, again effected without full argument. It is true that the general meaning was not in issue in *Harney* and further one recognises the busy agenda of the Court which must prevent it from too often indulging in full obiter discussion. However this is twice now that recklessness has received a somewhat superficial analysis. It is to be hoped that on the next occasion the issue will be fully canvassed. The issue at stake is an important one. For those who may think that it is merely an academic frolic, a reading of the case referred to by the Court in *Harney*, namely *Elliott v C* (1983) 77 Crim App R 103, will show it to be anything but.

So, where are we now? Recklessness will normally be subjective. However, taking a line through *Howe*, perhaps one should expect objective recklessness arguments when recklessness relates to only one part of an offence, and the other parts clearly involve moral blameworthiness. For example, in *Howe* the accused were first established to be rioting. The issue then turned on the level of awareness required as to whether the vehicle they were damaging was a Crown vehicle. For instance, did one need to actually know it was a Crown vehicle or would a lesser degree of awareness be sufficient? The Court of Appeal held that in these circumstances objective recklessness would suffice. In the main though, as Dawkins has argued ((1983) 10 NZULR 365), the statutory context, at least for express recklessness, will normally clearly suggest a subjective interpretation.

Finally, note should be made of the definition of subjective recklessness. The meaning suggested by the Court of Appeal in *Harney* is in no way the traditional definition and leans much more in favour of the accused. The test proposed is

> foresight of dangerous consequences that could well happen, together with an intention to continue the course of conduct regardless of the risk.

The notion of dangerous consequences is new; it appears to be a rewording of the traditional balancing requirement that it be unreasonable for the accused to run the foreseen risk. If what is foreseen must now involve dangerous consequences (to whom or to what?) then the concept has been considerably narrowed. Furthermore, the consequences must be ones which "could well happen". Again this seems an unwarranted narrowing: the traditional balancing concept allows greater flexibility. Previously risks that were unlikely to happen could still give rise to subjective recklessness if the accused had seen the risks and they were risks which carried severe consequences for little social gain. For example, it was regarded as unreasonable to run even the smallest chance of death, unless the act contained significant social utility. This new definition, if taken literally, will only capture situations of real risk and will rule out those where any risk, however slight, was unwarranted.

It is probable that the Court of Appeal did not intend to effect such a radical change in the definition of subjective recklessness. If this is so then the best definition to use remains that proffered by the English Law Commission Working Paper No 31 on the Mental Element in Crime.

> A person is reckless if (a) knowing that there is a risk that an event may result from his conduct or that a circumstance may exist, he takes that risk, and (b) it is unreasonable for him to take it having regard to the degree and nature of the risk which he knows to be present.

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Judicial review

Webster v Auckland Harbour Board, [1987] BCL 1254.

The saga of *Webster v Auckland Harbour Board* has finally come to an end. Administrative lawyers will recall that in the early stage of the proceedings the Court of Appeal declined to strike out the review application in limine. The Court of Appeal refused to hold that the respondent's decision to increase a licence fee for the continued use of part of the Auckland foreshore for a boat ramp was not capable of being described as the exercise of a "statutory power of decision", within the meaning of the Judicature Amendment Act 1972. The Court therefore rejected the argument that the decision to increase the licence fee, and the subsequent decision to revoke the licence, were done pursuant to "contractual" rather than "statutory" powers.

Then in the subsequent substantive proceedings Tompkins J confirmed that the respondent's decisions were indeed capable of being described as "statutory powers of decision". However, His Honour rejected the applicant's argument that the respondent board had acted either "unreasonably" (in the *Wednesbury Corporation* sense of the word) or "unfairly" in the exercise of those powers.

On appeal the Court of Appeal upheld the findings of Tompkins J. The appeal was therefore dismissed.

Judgments and comment

Public authorities and contract

The judgments of the Court of Appeal are worth briefly noting for three reasons. Firstly there is an important reaffirmation of the principle that in the exercise of contractual powers statutory bodies can be in a quite different situation from the private citizen. Cooke P took the opportunity of again citing Sir William Wade's view that unfettered discretion is wholly inappropriate to a public body. His Honour reiterated the view of his earlier joint judgment that even the exercise of contractual powers by public bodies is open to review by the Court on public law grounds, and he discountenanced the interpretation placed on that joint judgment by a subsequent, differently comprised Court of Appeal in *New Zealand Stock Exchange v Listed Companies Association* [1984] 1 NZLR 699.

It is now clear, therefore, that even when a public authority appears to be acting as if it were a private citizen in entering contracts it will in fact be subject to the administrative law grounds of review. In principle this is unexceptionable. For unlike the private citizen a public body has been created and is inherently limited by a statute enacted to promote the public good. As Casey J put it in this case:

> [t]he Board is a public body administering assets which it holds for the benefit of the public in its area and accordingly does not have an unfettered discretion in the exercise of the powers given to it under the Harbours Act.

Judicial restraint

The second point from the judgments will reassure any public authorities fearing excessive judicial intrusion into their contractual and management arrangements. Consistent with the comments made in the earlier judgments in the Court of Appeal (which were again quoted by Cooke P in this case), Bisson J warned intending applicants that

> . . . in review proceedings of the actions taken by a public body the Court's task is not to "monitor those actions" nor to adopt with hindsight a supervisory role in public administration.

To support his view of the need for judicial restraint in review proceedings of local public authorities, His Honour cited an important dictum of Lord Brightman in *Pulhofer v Hillingdon London Borough Council* [1986] AC 484, which had advocated such restraint. Thus whilst all the Judges in *Webster's* case were mildly critical of some shortcomings in "courtesy and frankness" on the part of the respondent, all the Judges were equally satisfied that the Board had, in the circumstances of the case, acted reasonably and fairly.

Unreasonableness

The reliance upon *Pulhofer* by Bisson J is of some interest. In that case Lord Brightman unequivocally adopted the view that unreasonableness is only available as a ground of review in administrative law where the unreasonableness verges upon "an absurdity" or, to put it another way, where the challenged public body is "acting perversely". Those tests were also employed by Bisson J, and represent the *Wednesbury* meaning of unreasonableness (see *Associated Provincial Picture Houses v Wednesbury Corporation* [1947] 2 All ER 680). Of course that interpretation of unreasonableness in administrative law is traditional and orthodox. But this reliance upon the *Wednesbury* meaning of unreasonableness by Bisson J is a little different from the interpretation of unreasonableness which is propounded by Cooke P.

It will be recalled that in 1986 Sir Robin Cooke had floated the view, extra-judicially, that "[v]ituperative epithets like perverse . . . seem . . . too emotive to be satisfactory as a criterion" (see M T Taggart(ed) *Judicial Review of Administrative Action in the 1980s* p 14). In his paper "The Struggle for Simplicity" Sir Robin had argued that the interests of simplicity required the Courts to accord "unreasonableness" its ordinary, straightforward meaning without any "distracting circumlocutions". The argument was supported by reference to such judgments of the House of Lords as *Wheeler v Leicester County Council* [1985] 2 All ER 1106 and *Bromley London Borough Council v Greater London Council* [1983] 1 AC 768.

However, subsequent to the delivery of that paper the House of Lords had forcefully reasserted the need to establish unreasonableness in the *Wednesbury* sense in a trio of cases: *In re Westminster City Council* [1986] AC 668, *Nottinghamshire County Council v Secretary of State for the Environment* [1986] AC 240 and *Pulhofer v Hillingdon London Borough Council* [1986] AC 484. Nevertheless the extra-judicial arguments heard from Sir Robin Cooke last year are found echoed in the judgment of Cooke P in *Webster's* case. The language is, of course, not as strong. The assurance is perhaps a little less. But in the course of his judgment Cooke P again rejected the usefulness of the *Wednesbury* terminology, and pleaded for a "steady and unvarnished adherence to the ordinary sense" of unreasonableness. His Honour explained that an "unreasonable decision is one outside the limits of

reason . . . one that no reasonable body could reach".

Some lawyers may well feel that with such a definition the argument is a debate over semantics, and lacks practical significance. Certainly in the present case both Bisson J and Cooke P reached exactly the same conclusions over the reasonableness of the respondent's action. Yet both judicial thinking and decisionmaking are inevitably influenced by the colour and force of the terminology adopted, and the adoption of the langugage of "perversity" and "absurdity" may well result in greater judicial restraint. Thus the recent House of Lords judgments could perhaps signal the beginning of the end of an era of judicial activism within the United Kingdom. Conversely Cooke P's continued advocacy of the "ordinary" meaning of unreasonableness could perhaps signal his desire to maintain the momentum of judicial activism within New Zealand.

Yet the judgments of Cooke P and the other Judges in this case do provide a useful reminder to administrative lawyers that the existence of wide grounds of review such as the duty to act fairly (or the duty to act reasonably) will not necessarily result in judgments in favour of the applicants. The case clearly shows that whatever idiom the Judges may use, they will require something more than minor "shortcomings" in administrative decisionmaking before they can be persuaded to interfere.

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Cheques "in full settlement"

There can be few questions in the law of contract of more practical importance than the question of whether a debt is extinguished by the debtor sending, and the creditor receiving, a cheque for less than the full amount accompanied by a letter or other communication indicating that the cheque is in full satisfaction of the debt. The question involves difficult matters of legal principle: for instance, if consideration be thought necessary for the discharge of a contractual obligation as much as for the creation of one, where is the consideration in such a case? It also raises complex issues of policy. On the one hand it is not fair for a creditor to renege on a promise to release part of his debt when the debtor has relied on that promise; on the other hand it is equally unfair for a debtor to hold a creditor to a promise of release which has been extracted from him in circumstances where the creditor needs ready money urgently.

The basic principle is still that confirmed in *Foakes v Beer* in 1884: a promise to accept a lesser sum in full satisfaction of a debt is not binding, and the creditor is able to sue for the balance. But the rule can work injustice, and has been buried in a thicket of exceptions, some of them logical and some of them not. New Zealand has a particularly effective statutory one – s 92 of the Judicature Act 1908 – which is far too often forgotten. But most of the exceptions are judge-made, and the most important of them is the one expounded by Mahon J in *Homeguard Products Ltd v Kiwi Packaging Ltd* [1981] 2 NZLR 322: if a debt is unliquidated, or if the amount of it is in dispute, the acceptance by the creditor of a lesser amount than he originally claimed is binding as a valid accord and satisfaction. Although there can be some difficulties of principle (what consideration does the debtor provide if the amount he has paid is the least that could possibly be owing?), there has been no serious doubt about the validity of Mahon J's general rule. But there has been much more doubt about another principle laid down by Mahon J. He appears to have decided that if a cheque for a lesser amount, accompanied by an indication that it is tendered in full settlement, is *banked by the creditor*, that alone is an irretrievable manifestation of his assent to the condition, and the debt is extinguished by accord and satisfaction. Thus the creditor has only two options: to bank the cheque and extinguish the debt, or send the cheque back.

This principle has been applied many times since *Homeguard*. District Court Judges have been bound by it, and High Court Judges have until recently followed it. Thus, in *Kirkland v Lindisfarne Landscapes Ltd* [1985] 2 NZLR 534 a debt was held to be extinguished when the creditor banked the cheque even though the very day before he had told the debtor he did not accept it as being in full settlement (although in that case the fact that the creditor had retained the cheque for three months before banking it may have had some bearing). And in *Broadlands Finance Ltd v St Johns Motors (Wanganui) Ltd* [1986] BCL 504 a creditor was similarly bound when, following common practice, an accounts clerk banked a cheque after detaching without reading the letter which accompanied it; the letter was sent "upstairs" where it was eventually read, with an understandably hostile reaction. In one or two cases (most notably *Brown v Reardon* [1985] 2 NZLR 350) *Homeguard* was grudgingly accepted but distinguished on slender grounds.

The *Homeguard* case seems, on this point, to be wrong in principle. If accord and satisfaction is based on agreement, the question whether the creditor has demonstrated agreement must surely in each case be a question of *fact*. No doubt sometimes the banking of a cheque without more will be evidence of assent to the condition. But it is difficult to see how agreement was present in *Kirkland* when the creditor had specifically *told* the debtor that his banking of the cheque was *not* to be taken as manifesting his assent to the extinction of the debt, or in *Broadlands* where the creditor seems not even to have known of the condition at the time the cheque was receipted. Morevoer experience suggests that the *Homeguard* case may well have induced some of the more wily debtors to "try it on" by, for example, attaching "full settlement" conditions to their cheques in the hope that their creditors would bank the cheques without realising the consequences.

Yet the fact is that Mahon J was simply applying a rule which has been established as common law in the United States. Although it is true that the Uniform Commercial Code has cast a little doubt on its continued validity, there is no doubt that the common law rule survived there for years. The American experience would suggest that once

the rule is established and well known, creditors have to regulate their businesses to cope with it, and the element of taking by surprise is less prevalent. The rule has at least the merit of certainty.

Yet, as stated, the *Homeguard* "rule" is very difficult to reconcile with contractual principle in that it converts what should be a question of fact into a question of law. It is therefore not surprising that commentators have been critical of *Homeguard* (see Russell (1984) 12 ABLR 301 and McLauchlan (1987) 12 NZULR 258) and that, eventually, the Courts have begun to question it, and indeed openly to disagree with it. There are two important recent High Court cases which appear to signal the turning of the tide.

The first is *Equitable Securities Ltd v Neil* [1987] BCL 576. A debtor owed money on both a first and a second mortgage to the same creditor. After a mortgagee's sale by the creditor as first mortgagee had failed to realise anything like the amount owing, the creditor agreed to accept from the debtor a lesser amount than the full amount owing on that mortgage. The debtor sent a cheque for that lesser amount "in full and final settlement re Equitable Securities Ltd". The creditor having banked this cheque, the debtor then alleged that this extinguished the debts under *both* mortgages. This plea failed, for two principal reasons. First, the debts were liquidated amounts, so there was no room for the doctrine of accord and satisfaction: *Foakes v Beer* applied, and *Homeguard* was not in point. Secondly, the condition attached to the cheque by the debtor did not clearly convey that it was meant to be in satisfaction of *both* mortgage debts: indeed the more rational interpretation in the light of the dealings between the parties was that it referred only to the first mortgage. Chilwell J accepted that before a condition can have effect it must be brought to the attention of the creditor, and here that had not been done, at least in the sense the debtor intended.

However, the case has two implications for *Homeguard*. The first is tnat Chilwell J stated that whether the recipient has accepted a cheque subject to a condition is a matter of inference from the facts, and it is clear that the state of knowledge of the recipient of a cheque or other bill of exchange is important. It is not easy to reconcile the *Homeguard* "rule of law" with such an approach. The second important feature of the case is that Chilwell J discussed at length s 21(1)(b) of the Bills of Exchange Act 1908. That provision reads:

> As between immediate parties . . . the delivery [of a bill of exchange] . . . (b) may be shown to have been conditional, or for a special purpose only, and not for the purpose of transferring the property in the bill.

In *Homeguard* Mahon J appears to have relied on this provision as additional support for his decision on the reasoning that a conditional cheque passes property only if the condition is accepted; and a creditor who banks a cheque will not be heard to say he does not accept the condition, for he would otherwise be confessing to conversion.

Chilwell J did not regard Mahon J as intending to lay down a binding precedent by this suggestion. Chilwell J regarded s 21(2)(b) as laying down no more than a rule of evidence: it enables parol evidence to be given that a cheque is subject to a condition.

> It does no more than that: it does not give a drawer any new right to impose a condition. Whether or not the delivery of a cheque is subject to a condition must always be a question of fact.

It must be said that, even after *Equitable Securities*, the exact effect of s 21(2)(b) in this context is unclear, and questions remain. Is a condition of the kind in *Homeguard* really capable by virtue of s 21(2)(b) of stopping property in the cheque passing to the creditor? If it is, and if a creditor is guilty of conversion in accepting the cheque but repudiating the condition, what relevance has that to the question of whether the whole debt is extinguished? At the very best, after the discussion in *Equitable Securities* the force of Mahon J's reliance on the subsection in *Homeguard* is diminished.

The other recent case is *HBF Dalgety Ltd v Morton* [1987] BCL 984. Dalgetys acted for Morton in the sale of his farm and sent an invoice for commission of $9,786. Morton sent them a cheque and the invoice, on which he had written the words "my estimate of costs on a 'work done' basis $2,450". Dalgetys banked the cheque, and sent a letter saying that the account was not accepted in full satisfaction. (Unfortunately this letter was not produced in evidence.) It was held that Dalgetys were not debarred from claiming the balance of their commission. Hillyer J based his decision on two grounds.

The first ground was that for accord and satisfaction to be established there must be a genuine dispute: it is not sufficient that the debtor merely be reluctant to pay. In this case Hillyer J found there was not a genuine dispute. The commission had been accurately calculated in accordance with the real estate agents' scale, and there was no proper basis for the debtor's attitude. This is an important finding, for there has been little discussion in the earlier cases of what amounts to a "dispute" in this context. There can be no doubt that the minimum requirement is bona fides on the part of the debtor; it is not certain whether one has to go further and show that the debtor's argument has at least some substantive merit. This point was discussed in the context of compromise of suit, without finality being reached, in *Couch v Branch Investments (1969) Ltd* [1980] 2 NZLR 314. In this respect Hillyer J's "no proper basis" finding may be significant.

The second ground for the decision was that for accord and satisfaction to operate the parties' agreement must be clearly spelt out. The debtor must clearly have conveyed to the creditor that his cheque was tendered in full satisfaction. That was not established here. The debtor's somewhat cryptic statement on his invoice was not a sufficiently unequivocal indication that $2,450 was all he was going to pay.

> It is, I think, reading into the statement far more than is there to say it means that the amount can be taken only if it is accepted in full and final settlement.

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Training the lawyer for the Courtroom

By Judge Anand Satyanand of Auckland

Judge Anand Satyanand was a Section Leader in the pilot Litigation Skills Programme conducted by the New Zealand Law Society at Porirua in 1986. Whilst on study leave in 1987 he attended two advanced advocacy skills teaching courses in the United States. He has written this article describing the teaching method developed for use in the New Zealand programme.

To ask the question "What are the essential lawyerly skills for the Courtroom?" of a member of the legal community, is to invite an answer which will undoubtedly take time, and which will cover many things.

The question and answer make one sympathetic to the observation of Lord Justice James, who in answering such a question in *Panama v South Pacific Telegraph* (1875) L R 10 Ch App 526 said "The clearer a thing is, the more difficult it is to find an express authority or any dictum, exactly to the point".

Differences of opinion and focus will occur, dependent upon the nature and disposition of the interviewee. Yet the question is one which registers prominently in the mind of the law student or tyro lawyer wishing to make a success of his or her chosen career.

The provision of the answer – that of teaching courtroom skills – is one which has had indifferent success in recent times. Neither the law school, nor the modern law office are geared up with sufficient expertise to focus on this field precisely enough. They (law school and law office) are doing other things better. That state of affairs has led to what is perceived to be a decline in advocacy skills in our Courts. The trend has caused many lawyers and Judges to seek to do something about reversing the process, and to set up again, standards of quality and excellence, from which the general community can benefit, and from which the legal community can take pride.

Essential skills

The essential lawyerly skills, it will be agreed, include analysis, organisation, verbal dexterity, integrity, judgment, persuasion and veracity, in an order which a short paper does not permit the space to determine.

If asked to submit one word as underpinning *the* essential lawyerly attribute this writer would submit the word "self criticism" or "self evaluation" in the sense that the better lawyer is the person who can interpret any situation accurately and mount his or her next action accordingly. This, of course, leans over towards the rather delicate area of personal foibles and characteristics, and adds to the problem of skills teaching in this field.

The foregoing is not a problem restricted to New Zealand. In the United States in the early 1970s the then Chief Justice complained bitterly about the decline in skills and competence of lawyers appearing in Courts throughout that country.

As a consequence, lawyers and Judges combined to form the National Institute for Trial Advocacy which began practical teaching courses to simulate trial experience. Over the succeeding years, the training techniques developed by NITA have been refined and widely copied. The techniques have been adapted as teaching tools in many independent courses.

The concept reached New Zealand through a pilot programme conducted in 1986. Fifty New Zealand lawyers went through a NITA type course conducted by a well known US advocacy teacher and trial lawyer, assisted by a number of New Zealand Judges and experienced counsel. Upon evaluation, the course was adjudged a success and a series of decisions were taken to proceed with a New Zealand initiative in the teaching of advocacy skills – with our own adapted materials, teachers and textbooks.

In recent years the NITA course developers have made a particular effort to isolate the factors that promote good simulated trial training. NITA conducts regular courses through the US for young lawyers. In each year as well NITA conducts courses at Harvard and Berkeley to train teachers of trial skills in the techniques.

The purpose of this article is to explain the teaching method to the general New Zealand reader of legal publications.

Learning by doing

The key element in training is an emphasis on *learning by doing* on the part of the student/lawyer. Lectures simply describing trial methods are not successful. The student/lawyers must participate to

a greater extent than the teacher. The student is called upon to attempt repeated exercises of examination-in-chief and cross examination and so on to all parts of the trial. Many repeat performances of five minute exercises followed by brief, pointed critique by knowledgeable trial lawyers who form the faculty, is the key to the process. Growth occurs rapidly through this means and it is superior, educationally, to an occasional lengthy exercise.

In the trial training programme, therefore, each student is given an opportunity to perform several times a day, throughout a concentrated five day period. Moreover each student/lawyer learns by observing his or her contemporaries perform portions of the same exercises.

Reduced to simple terms, the courses equate the learning of courtroom skills such as leading of evidence, cross examination, presenting exhibits to the Court through a witness, and/or making addresses and submissions to skills which can be taught like teaching someone to ride a bicycle. The teaching of skill requires demonstrations, actual attempt or performance by the learners, critique or assistance by the teacher, and immediate repeat of performance by the student hopefully with an improvement each time.

Courses and exercises are designed to simulate both in volume and complexity live courtroom and office practice. Before commencement, students receive and are required to assimilate a case file which may consist of a factual summary, witness statements, photographs, plans and a reference to appropriate statutes or judgments. The student is required to have prepared the facts so as to be able to lead examination-in-chief or to cross-examine or to address the jury. The course is self contained so that the preparation must extend to the student being able to perform the role of witness or counsel in the case.

Importance of the critique

The nature of the critique, which is the key teaching element, is extremely important. Ironically, however, many trial lawyers are poor critiquers, until they have received some training and practice in the skill of critiquing. Most experienced trial lawyers have an intuitive sense that a particular examination-in-chief or cross-examination would have been successful or unsuccessful with a Judge or jury. However, their ability to articulate in specific terms exactly why the exercise would have been more or less successful is often lacking.

Lawyers may preface a critique with a remark such as "That was good but . . .". That sort of preface does not necessarily assist the student. Other critiquers believe they must reduce the student/lawyer virtually to tears — but such are destructive rather than educational. Some critiquers tell "war stories" — apparently believing that the student will easily see the relationship between the critiquers' past experience and the exercise at hand. The stories are often entertaining, but they consume valuable time (which is better used by student exercises) and the point is often lost on the students. War stories should accordingly be saved for the dining and bar rooms. Other critiquers can tend to be conclusory. For example, "Jane, that was a pretty good cross-examination, but you should use more leading questions on cross-examination and not let the witness evade answering you". This example fails to particularise how the student should change. Other critiquers might run through an extensive list of observations, listing 10, 15 or even 20 points which they observed during the examination. This type of critiquing would be lost on any student attempting to learn.

Brevity and diagnosis

Before proceeding to describe the technology of teaching in this fashion, there are two key words that underlie everything which is involved. Those key words are brevity and diagnosis. The critiquer should choose one or two major points on which to critique the student. As we all know from Courtroom experience, overload sets in very quickly if too much is attempted at one time. It is important to key into the point to be covered. If the teacher encounters a problem in choosing the appropriate point, a question or two asked of the student lawyer will often clarify this.

As the student will be attempting similar exercises on a repeated basis throughout the course, there is no need to critique on every point during each exercise.

Moreover, the student will be observing other students and other points can be saved for those students. These points will register with the first student. The critiquer should be mindful of teaching the group as a whole. Thus, one may decide to critique a point for its value to the entire group, although the particular student had other weaknesses.

In the teaching model, team teaching is the rule. That is, two faculty members are generally present with eight students. If each faculty member covers two points then, each student, for each five minute exercise, will have been critiqued on four points. Thus, simply critiquing on one or two points maximum, but doing it properly, is most valuable.

The test of a good critique seems to be the answer to the question "Will the student improve the exercise on his or her next attempt?" The emphasis is on improvement by the student; not on showing off the faculty's skills.

Four elements

The NITA method has developed four elements for a good critique on a single point following appropriate diagnosis: *Headnote, Playback, Prescription* and *Inquiry.*

A good critique should begin with a *headnote.* An example of a good headnote is as follows: "Jane, I'd like to discuss your failure to use leading questions during the cross-examination. A good cross-examination will consist mostly of leading questions which tightly control the witness and thus limit his ability to give evasive answers." This headnote succinctly focuses the student on one key aspect of cross-examination and the reasons for it. The student/lawyer now knows the exact subject of the critique, and the reason for its importance.

The second element of critique is *playback.* Playback is a specific recital of the specific shortcoming in the performance by the student/lawyer. The best playback is the verbatim repetition of the questions and/or answers on which

the critiquer is focusing. "Jane, during your cross-examination you used non-leading questions: 'What did you say about meeting an investigator?' 'What did you say about giving the insurance assessor a statement?' 'What did you say to that person about the red light?' " By giving that kind of specific replay or playback, the student knows exactly the portion of the cross-examination to revise on her next time.

Third, the critique should give a *prescription* for revision of the cross-examination. "Jane, when you perform your next cross-examination, I want you to be sure each question is phrased in a leading fashion." The most controlling form of a leading question is not really a question at all. Rather, it is a statement with a questioning inflection. For example, questions could be phrased as follows: "You were then seen by the insurance assessor?" "You then signed a statement?" "This is your signature, right?" "This statement says at Line 4 — 'The light was green.' ". This form of prescription is known as the mini-demonstration and is rated as being of exceptional value as a teaching aid. First, it is precise and to the point. Secondly, it implicitly demonstrates to the student that the faculty member can perform a competent cross-examination — thus underlining the instructor's credibility. Thirdly, the student/lawyer knows precisely how to correct the deficiency.

The final element of a good critique is *inquiry* and can often be delivered by the second critiquer. The student lawyers can be asked how they might change their performance based on the critiques they have just received from the first critiquer. The student lawyer may also be asked to repeat a brief segment of the exercise to test whether the critique has been understood. Inquiry is also an excellent method of testing the critiquer because if the critique has been vague and nonspecific, the student will invariably be unable to respond to the inquiry.

Improving performances

Critiques that follow this model have been demonstrated to truly assist the young Court lawyer to improve his or her performances in all aspects of trial within a very short period of time. Such critiques are forward-looking and provide models for future exercises. In addition, because they are to the point and brief, they will allow all students to pick up rapidly on the points and to participate to a greater extent in the opportunity to perform various exercises, thus creating more opportunities for learning by doing. Teachers should always remember the time constraints and the need to keep moving. A student/lawyer performance of up to ten minutes should be followed by the two critiques each taking up to, but not more than, two and a half minutes each.

Of course, each critique depends on the lawyer/teacher making first an accurate diagnosis of a deficiency. Diagnosis will depend on and vary with the level of the student/lawyer. It is recommended that the critiquer listen carefully and take verbatim notes of important points and discuss with the student using the recommended format the point(s) which are the most important for this student at his or her level of skill. It is preferable to save the more complex points for a later day.

A major component of the teaching method is video tape review. Each student/lawyer performance is videotaped. The student, after critiquing by the faculty in a small group, is later reviewed by a separate faculty member who did not observe the live performance. This gives the student an opportunity actually to observe the playback for himself or herself. Of greater benefits perhaps, is the opportunity to observe oneself as a jury, Judge or opponent might see one. Simply observing oneself on tape and observing one's progress throughout the programme is, in itself, an extremely valuable thing for most beginning advocates. The videotaped critiquing usually takes place in a private room. It therefore gives the critiquer and the student the opportunity to discuss in frank terms, personal mannerisms, habits, voice, dress and other intangibles which may be areas of sensitivity for the student/lawyers. The videotape should be preserved throughout the programme so that at the end of programme, a student, by watching the whole tape, can literally see clear progress from the first day to the last.

There is accordingly a contrast — the live review critique concentrates upon matters of substance and the video review critique upon matters of form or style.

The programme begins with demonstrations and lectures by experienced trial lawyers to establish an appropriate model. Although valuable, this portion of the programme is less real to the students until they have "had a go" themselves. Each demonstration should be followed by an opportunity for the students to question the demonstrator(s). The problem should be one the students have familiarised themselves with so they can readily identify with the demonstration and ask pointed questions of the demonstrator(s). These demonstrations are important because they allow the faculty to establish that they can do what they are talking about. It is critical for the student lawyers to believe at an early stage in a programme that the faculty they are working with, is capable of performing the exercises which they, the learners, are attempting.

Two workshops

Team teaching is an important concept in this model of instruction. The idea is to have students exposed to experienced trial practitioners as well as trial Judges and trial advocacy teachers during a programme. During each workshop, two instructors are present, and work together. The idea is to complement each other without repeating comments, arguing or competing. Many trial lawyers have difficulty in learning to accept the limits of their roles as team teachers, but the teaching model is an important concept and the faculty is enjoined to use it at all times. If the first critiquer covers the point intended to be covered by the second teacher, no critique should be given — the class should move to the next student. Critiquers are asked not to encroach upon the time of the student/lawyers or fellow teachers. No critique should exceed the length of the student exercise in the classroom. Lengthy discussions are

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Contracts: penalties

By S Dukeson, a Whangarei practitioner

Discount clauses on rebate clauses in contracts raise the problem of the legal implications of penalties. In this article the author looks at a recent English decision and suggests it takes an unnecessarily strict technical attitude by comparison with the slightly earlier New Zealand case of Marac Finance Ltd v Turner.

The Lombard Case

As is demonstrated by a recent case, the approach of the English Courts to penalty and liquidated damages clauses appears to be much more technical than that of the New Zealand Courts.

In *Lombard North Central plc v Butterworth* [1987] 1 All ER 267, the plaintiff Finance Company leased a computer to the defendant. The defendant failed to pay a series of instalments promptly (time being of the essence) and on a number of occasions failed to make any payments. Pursuant to a contractual right, the plaintiff terminated the agreement.

On termination, cl 6 of the agreement purported to allow the plaintiff to recover all arrears of instalments and all future instalments. The plaintiff accordingly brought an action to recover those sums or alternatively, damages for breach of contract.

The Court of Appeal held that in the absence of a repudiatory breach, cl 6 constituted a penalty and was unenforceable. The fact that the clause provided for a discount or rebate was considered to be irrelevant to the penalty issue. On the facts, it was held that the failure to pay instalments did not amount to a repudiation. Nevertheless, it was held that because cl 2(a) made time of the essence with respect to the payment of instalments and because the plaintiff had the right to terminate the agreement for the defendant's failure to pay instalments, the defendant's breach went to the root of the contract and the plaintiff was entitled to recover damages for the loss of the whole transaction.

Financings Limited v Baldock

Nicholls LJ (with whom the other Judges agreed) dealt with the penalty question in detail. He referred in particular to *Financings Limited v Baldock* [1962] 2 QB 104. In that case, the agreement enabled the owner to terminate the agreement (inter alia) if the hirer failed to pay any instalment within ten days after the due date. Time was not expressly made of the essence. On termination, the hirer had to pay such amount as would make the total payments paid by the hirer under the agreement equal to two-thirds of the total hiring cost "as agreed compensation for the depreciation of the goods" or the amount of all instalments and other moneys due at that time, whichever was greater. The clause was held to be a penalty, there being no repudiation by the hirer, and the owner was entitled to recover damages only for breach up to the date of termination. It was Lord Denning's judgment that was cited with approval by Nicholls LJ in *Lombard*. Lord Denning said:

> [When] an agreement of hiring is terminated by virtue of a power contained in it, and the owner retakes the vehicle, he can recover damages for any breach up to the date of termination but not for any breach thereafter, for the simple reason that there are no breaches thereafter. I see no difference in this respect between the letting of a vehicle on hire and the letting of

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best saved for the video tape review.

An important aspect of any programme is the use of a building-block approach. Problems and exercises must be carefully selected and sequenced so the student lawyers progress in developing skills throughout the programme. For example, the first examinations-in-chief simply focus on training the student to gain comfort using simple, non-leading questions to create a word picture. Students are then encouraged to go on to introduce exhibits. Complications, such as exhibit foundations, use of leading questions on examination-in-chief, refreshing recollections, and hostile witness handling techniques follow after the students have demonstrated an ability to ask clear, direct and simple questions. The same progression is used to develop cross-examination skills.

The programme itself should progress, too. Several days of examination-in-chief and cross-examination and addressing the jury are furnished in the set exercises, progressing from the most simple to more complex tasks. Nearer the end of the programme the students interrogate expert witnesses and attempt more advanced skills. The programme concludes with a one day jury trial and the students watch "their" jurors deliberate on a remote video monitor.

The entire process is thus something where teaching and learning go hand in hand by both student lawyer and teacher. It should sensitise the student towards self-evaluation and analysis of those essential lawyerly skills.

Mastering several skills

Good training of the advocate, like good advocacy itself, is an art dependent on the mastering of several skills. Those skills can only be developed with practice and with thought and reflection over an extended time. □

land on a lease. If a lessor, under a proviso for re-entry, re-enters on the ground of non-payment of rent or of disrepair, he gets the arrears of rent up to the date of re-entry and damages for want of repair at that date, but he does not get damages for loss of rent thereafter or for breaches of repair thereafter.

In this and many hire-purchase agreements the owners have sought to avoid that general principle by inserting a "minimum payment" clause. . . . [Such] a clause is now held to be a penalty clause. The owners by such a clause are really seeking, on an early termination of the hiring, to recover damages for loss of future rentals when they have not lost any. They have no right to future rentals after they have terminated the agreement and got the vehicle back. (ibid p 110-111)

Lord Denning (ibid p 112) then referred to the judgment of Salter J in *Elsey & Co Limited v Hyde* (unreported). Salter J stated that the reason why the hirer could not recover expectation damages when the owner terminated the agreement pursuant to a contractual right was because:

> The reason that they have suffered is that they have secondhand goods put on their hands before they have received very much money in respect of them. That is not the result of the hirer's breach of contract, in being late in his payments, it is the result of their own election to determine the hiring.

Finally, Lord Denning referred to authorities (*Yeoman Credit Limited v Waragowski* [1961] 1 WLR 1124; *Overstone Limited v Shipway* [1962] 1 WLR 117) which had allowed the owner to recover expectation damages. Lord Denning distinguished these authorities on the basis that they had involved repudiations by the hirer but nevertheless felt that they were indefensible conceptually because, irrespective of the repudiation, in each case the owner had a contractual right to terminate the agreements for the hirer's failure to pay instalments. Lord Denning did not see why the owner should be in a better position to recover expectation damages simply because of a repudiation.

Trivial breaches and penalties

When the owner has been given the right to terminate the agreement for any breach, so that every term or every breach has been made essential, it might be thought to be somewhat misconceived for a Court of equity to assert that a minimum payment clause is a penalty, based on the premise that the owner has been given the right to terminate a contract for any breach "no matter how trivial". The apparent misconception is resolved on the basis that the Court of equity looks behind the expression of the parties' agreement so that if the owner has been given the right to terminate a contract and recover a minimum payment for what might be *in fact* a trivial breach, equity will regard the minimum payment clause as a penalty.

Repudiation and penalties

To say that a minimum payment clause will be a penalty in the absence of a repudiation is surely misconceived. The question of whether a clause is a penalty or not is to be determined at the time when the contract was entered into. Subsequent events, including repudiations, must be irrelevant. Accordingly, it is submitted that it is incorrect to assert that a repudiation will prevent a clause from being a penalty (and effectively convert it into a liquidated damages clause).

There seems to be some confusion in these cases surrounding the concept of repudiation. For example, in *Lombard*, Nicholls LJ, having found that there was no repudiation, then proceeded to find that there had been a breach going to the root of the contract which amounted to a repudiation or could be accepted as a repudiation. The concepts of a breach of "condition" and repudiation are distinct and there is no justification for this poor use of terminology. It may be that the statement that a repudiation will prevent a clause from being a penalty is simply an example of this poor use of terminology. It may be that all that is really intended to be by this statement is that even if a clause is a penalty, if there has been a repudiation, expectation damages will be recoverable. If so, this again demonstrates the point that the penalty issue and the damages issue are conceptually distinct.

Discounts, rebates and penalties

The trend in the English cases has been to state that a minimum payment claue will be a penalty clause (in the absence of a repudiatory breach) irrespective of whether it incorporates a discount or rebate in favour of the hirer. In *Lombard*, Nicholls LJ considered that if the *presence* of a discount or rebate was considered to be relevant, then the *absence* of a discount or rebate would mean that a minimum payment clause would be a penalty and that the owner would be limited to recovering (by way of damages) payments in arrears as at the date of termination (ibid p 275). Nicholls LJ considered that this would be wrong because he recognised that there would be cases (eg a breach going to the root of the contract) where an owner would be able to recover expectation damages.

It is submitted that the Judge's reasoning is misconceived. Even if a clause is held to be a penalty, it does not follow that any damages recoverable should be limited to payments in arrears. If a penalty clause does not mark the ceiling of recovery of damages (and it is submitted that the weight of authority suggests that it does not) there is no reason in principle why expectation damages should not be recoverable subject to the usual causation and remoteness tests.

It is important to keep separate the issues of whether a clause is a penalty and if so, what damages are recoverable. The first issue revolves around equitable considerations while the second issue concerns considerations of law. With respect to the penalty issue, the writer would have thought that the presence or absence of a discount or rebate would be relevant in determining whether a minimum payment clause was or was not a genuine pre-estimate of loss. Casey J seems to have thought so in *Marac Finance Limited v Turner* (A1225/80, 26/7/83, noted [1983] NZLJ 322).

Expectation damages and penalties

As has been stated, in *Financings Limited v Baldock* (supra), once the Court of Appeal had decided that

the minimum payment clause was a penalty and that there had been no repudiation, it limited the damages recoverable by the owner to an amount equivalent to the arrears of instalments together with interest. Despite the fact that the Court of Appeal in *Lombard* also considered that the minimum payment clause in that case was a penalty and that there had been no repudiation, it nevertheless considered that there had been a breach going to the root of the contract and that the owner was therefore entitled to recover expectation damages. Mustill LJ stated that there was nothing wrong with the parties making every term of the contract or every breach of every term essential and giving the owner the right to terminate for any breach of contract (ibid, p 273).

It is submitted that there is an inconsistency between the two cases. Lord Denning's judgment in *Financings Limited v Baldock* (supra) was cited with full approval in *Lombard* yet both Lord Denning and Lord Upjohn (in *Financings Limited v Baldock* (supra)) were of the opinion that in the absence of a repudiatory breach, expectation damages could not be awarded. (It is possible that Lord Diplock recognised that expectation damages could be awarded in the case of a breach going to the root of the contract not amounting to a repudiation (ibid p 120).

The two cases could be distinguished on the basis that in *Lombard*, time was expressly made of the essence with respect to the rental payments (so that, despite the fact that the minimum payment clause was held to be a penalty, failure to make payments on time would be a breach going to the root of the contract). Nevertheless, because at least two of the three Judges in *Financings Limited v Baldock* (supra) did not even contemplate that expectation damages could be recovered in the absence of a repudiation, *Lombard* is both inconsistent with and, it is submitted, represents an advance on that case (although the writer would not have thought that there was anything conceptually remarkable about this "advance").

Lord Denning's judgment in *Financings Limited v Baldock*

Because Lord Denning's judgment in *Financings Limited v Baldock* (supra) was cited with approval in *Lombard*, it may be worthwhile to consider his judgment in some detail.

As has been stated, Lord Denning considered that if a clause was a penalty, the owner could not recover expectation damages in the absence of a repudiatory breach. Lord Denning justified this first by drawing an analogy to leases of land and secondly, by stating that the owner could not recover damages for any breach after the date of termination (because there are no breaches after that date).

So far as the analogy to leases of land is concerned, there has been a recent trend, particularly in New Zealand but also in some other jurisdictions, to apply general contractual principles to leases. One of the most important aspects of this trend has been to allow a landlord to recover expectation damages after terminating a lease. In the writer's view, this is the correct approach to adopt in modern times. Accordingly, the writer would assume that (at least in New Zealand) damages questions with respect to leases of land would generally be dealt with in the same way as damages questions with respect to any other types of contract. Lord Denning's analogy would therefore be inappropriate in New Zealand.

Even if leases of land were (for historical reasons) considered to be special contracts of hire, with the consequence that expectation damages should not be recoverable upon termination, it is submitted that there is nothing special or exceptional about leases of chattels that require anything other than a purely contractual treatment to be adopted.

More important, it does not follow, in the writer's view, that because there are no breaches after termination that expectation damages cannot be recovered. First, there will obviously be no breaches after termination — the contract has been terminated! Secondly, if the intention behind termination in these situations is that the owner is to be discharged de futuro (and not to rescind the agreement ab initio) there is no logical justification for restricting damages to the reliance on restitution interests. Thirdly, it is surely incorrect to assert that where the owner terminates the agreement, the cause of the owner's loss is the termination and not the breach by the hirer. If this can be said about contracts of hire, it can really be said about all contracts which are terminated for breach. As the Court of Appeal in *Lombard* recognised, the parties are free to stipulate what breaches go to the root of the contract and if they effectively stipulate that every breach will go to the root of the contract, it would be a nonsense, as a matter of law, to say that it is the owner's election to terminate the contract that is the cause of loss and not the breach.

Marac Finance Limited v Turner

The only relatively recent New Zealand case that the writer is aware of which has discussed penalties in any detail was *Marac Finance Limited v Turner* (supra). The writer has previously noted the case in this *Journal* and for the present, simply notes that the approach of Casey J was remarkably simple compared to the approach taken by the English Courts. The emphasis in the *Marac Finance* case with respect to the penalty issue was on whether the clause constituted a genuine pre-estimate of loss. As has been stated, on the facts, Casey J held that the clause was a penalty but he indicated that had the clause provided for a rebate or discount, it may not have been objectionable. This view contrasts with the view of the English Judges. With respect, the writer prefers the simple approach taken by Casey J.

Summary

There are two issues with respect to a minimum payment clause. The first is whether it constitutes a penalty. In this regard, it is submitted that it would be relevant to enquire whether or not the owner has been given the right to terminate for any breach of contract (and possibly, on the happening of other events which might not amount to breaches of contract) and whether the minimum payment clause provides for a discount or rebate. If it is determined that the clause is in the nature of a penalty, the second issue is whether the penalty clause marks the ceiling of recovery. If not, it is submitted that, in principle,

expectation damages should be recoverable by the owner subject to the usual rules relating to causation and remoteness of damage (and of course subject to any specific statutory provisions). Such a result may well be abhorrent to our increasingly consumer-protection orientated society, but that is a matter for the attention of our legislature.

Addendum

Since this casenote was dictated, the writer has had the opportunity to read the decision of Smellie J in *General Finance Acceptance Limited v Melrose* [1987] BCL 1265.

The plaintiffs leased a computer to the defendant. The cost of the computer plus interest thereon amounted to $30,420.00 and was payable by equal monthly instalments of rental over a period of five years.

Clause 14 of the Agreement gave the Lessor the right to terminate the Agreement and to repossess the computer if the Lessee defaulted. In that case, Cl 15 provided for the value of the computer to be ascertained; for the value of any insurance moneys received by the Lessor to be ascertained and to be added to the value of the computer; for the amount of the payments yet to be made under the lease to be ascertained; and if the value of the computer plus the insurance moneys exceeded the moneys yet to be paid by the Lessee, then the Lessor would pay the balance to the Lessee and if the moneys to be paid by the Lessee under the Lease exceeded the value of the computer plus insurance moneys, then the Lessee would pay the balance to the Lessor.

After a relatively short period of time, the Lessee defaulted, the computer was repossessed and the Lessor sought to recover $34,710.48 either by way of the accelerated payment clause or by way of damages. The figure of $34,710.48 was made up of the total rental, less rent paid, less the value of the computer plus interest.

On the penalty issue, the Judge relied mainly on Australian authorities (to which the writer does not presently have access). The Judge noted that Cl 15 of the Agreement contained no discount for acceleration of payment of rental. (It would seem that it was not argued that the provision for giving the Lessee credit for the value of the computer and insurance moneys itself constituted a discount. However, such an argument would probably have been to no avail. Even if a credit for these items would have constituted a discount, it seems clear that it would not have been considered to be a sufficient discount to prevent the accelerated payment clause from being a penalty.)

It was accepted that the plaintiff was entitled to recover damages equivalent to the unpaid rental, less a proper value for the computer, and also interest (but not at the rate claimed). The plaintiff was not shown to have failed to mitigate its loss.

The writer mentions the case for several reasons. First the writer criticised *Lombard* (supra) because of the complicated way in which the penalty and damages issues were approached in that case. *General Finance Acceptance Limited* (supra), like *Marac Finance Limited v Turner* (Al 225/80, 26/7/83), appears to have been argued and decided in a much less complicated way and it is again submitted that the New Zealand approach is preferable.

Secondly, it seems to be implicit in Smellie J's judgment that had the accelerated payment clause contained a discount for acceleration, what was otherwise a penalty might not have been a penalty. Contrary to the English authorities, the writer has submitted that the presence or absence of a discount provision is relevant in determining whether a clause is a penalty or not.

Because the Judge considered that there had been a repudiation, it was not necessary to consider what right a Lessor has to obtain damages if an accelerated payment clause or a minimum payment clause is held to be a penalty and if there has been no repudiation. □

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However there was a third ground on which Hillyer J would have been prepared to base his decision and it is the most important. He held that whether there is accord and satisfaction is a question of fact.

> If the question is one of fact, there will be accord and satisfaction only if there is a meeting of two minds, or if one of the persons involved acts in such a way as to induce the other to think the money is taken in satisfaction of the claim. But if the creditor does not agree, and if at the time that he accepts the amount he makes it clear to the debtor that he is not accepting it in full satisfaction, it seems to me that it cannot be said that there has been accord and satisfaction. If there were a rule of law that acceptance of a cheque is conclusive evidence of assent to the conditions on which the cheque was sent, the matter would no longer be a question of fact, but of law.

Hillyer J referred to Professor McLauchlan's article (cited above) and the authorities cited in it. He noted that nothing in the Court of Appeal case *James Wallace Pty Ltd v William Cable Ltd* [1980] 2 NZLR 187 was contrary to his conclusion, and expressly disagreed with the High Court cases which had applied the *Homeguard* principle. There was, he said, no basis for holding that the mere banking of a cheque is conclusive evidence of an agreement to accept it in full satisfaction. He concluded that in this case, provided the creditor could establish that it sent a letter when it received and banked the cheque, and that that letter made it clear that the banking was not an acceptance of the "full satisfaction" condition, "that letter would have prevented the appellant being bound to accept the smaller amount in lieu of the larger".

It will be interesting to see what line future Courts will take. There is now a conflict of approach in the High Court, but in view of the criticism to which *Homeguard* has been subjected, and the convincing reasoning in the *Dalgety* case, it is likely that this most recent authority will preferred.

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The tax adviser:

Responsibilities and liabilities of the professions (I)

By Anthony Molloy QC, LLD of Auckland

This is the first part of an article which looks at the responsibilities and liabilities of members of the legal and other professions when giving tax advice. In view of the growing importance of taxation law this article and the subsequent one are very significant in terms of current professional practice.

The duty to advise

We have it on impeccable authority that

i it is the right of the businessman, and the duty of the company director, to consider lawful means by which to minimise tax: cf *IRC v Burmah Oil Co* (1981) 54 TC 200, 220D per Lord Fraser of Tullybelton (HL, Sc).

ii it is negligence for those tendering advice to businessmen or companies to ignore or overlook the tax consequences of commercial proposals: cf *Tayles v CIR* [1982] 2 NZLR 726, 728, lines 9-10 per Cooke J (CA).

Duty remains, even in respect of a proposed artificial avoidance scheme or a proposed sham.

It would also seem to be uncontentious that, if a scheme is put to an adviser which is highly artificial, or even a sham or a fraud, the client remains entitled to advice.

The nature of the advice that can be given in such circumstances may be severely qualified, as I shall suggest later in more detail.

But to the extent to which the proposed scheme is legal, the client is entitled to be told how to do it, and what to avoid. And in all cases, whether the proposal is legal or not, the client is entitled to expect advice as to his rights in law; as to any alternatives lawfully open to him; and as to the adverse fiscal or penal consequences, as well as the advantages, of the adoption of each of those alternatives.

The ethical corollary of the duty to advise

The client has a right to this advice, and a right to be indemnified if it is negligently given and causes him damage, only because there rests on the lawyer a professional duty to give the advice.

If the matter is seen as one of duty, then it must follow, not only that is it ethical to advise, even on artificial schemes or shams, but that it would be positively unethical for the lawyer professing tax as among his fields of practice not to do so.

Whether advice to be confined to technicalities

Because Courts are concerned with legality, not morality, it does not befit the judiciary to pass public moral censure on the efforts of the subject to avoid tax if he can do so without dishonesty. But lawyers and accountants impoverish the very concept of a professional if their private advice to clients is straitjacketed by purely technical considerations.

These technical considerations must be canvassed, of course, and with all diligence. The client is entitled to hear whether the proposal is lawful, or whether he will break the law if he proceeds; whether it complies with accounting standards, or whether those standards will be infringed or even reduced to tatters.

But the client surely is entitled to more than this. He is entitled to counsel on the matter generally. He has a right to have his perspective enlarged, or even corrected.

Mr Elliott Richardson was a distinguished United States lawyer and statesman. He resigned office as Attorney-General of his country sooner than obey President Nixon's ukase that Mr Archibald Cox be fired as Chief Watergate investigator. Richardson addressed some comments to the US Bar Association in Honolulu in 1974 and expressed the view that

> We are not the keepers of our clients' consciences, but neither are we mere technicians whose sole function is to assure that legal limitations are narrowly observed. The attribute of our calling which most entitles it to

> be regarded as a profession springs from the fact that our highest allegiance is to the law and to our own consciences – and of the two our own consciences are the more inclusive, though not necessarily the higher, authority. We fulfill the highest standards of our profession when our informed legal opinion is supplemented by judicious counsel. Without undertaking to preach to our clients, we can encourage them to ask not just 'is it legal?' but 'is it right?'
>
> The claim of what is right over what is merely legal, of unenforceable obligations over enforceable rights, is not exclusively addressed, of course, to [the legal] profession. But it is an appeal, essentially, for moral leadership, and we cannot, although some would disagree, plead a lack either of competence or of jurisdiction. ("The Mindless Slide" [1975] NZLJ 144, 147.)

I do not believe accountants should have their sights set any lower than this, either.

Members of either profession betray both their clients and the community if they fail at least to attempt to temper the excitement and enthusiasm of a client who has discovered, or thinks he has discovered, a means for exploiting a tax loophole, and conducting a raid on the Consolidated Fund, in an exercise which will be commercially barren, artificial, and contrary to any concept of good citizenship, even if it will not necessarily be unlawful.

Of course, if, having received this advice, the client insists on proceeding with such a scheme, the adviser's duty clearly is to give all necessary technical advice and assistance in furtherance of the client's interests. (cf *Leary v FCT* (1980) 47 FLR 414, 434 per Brennan J (Full Federal Court))

Limits on the scope of advice when the proposed scheme extends to illegality

If the client's proposed scheme goes beyond the merely commercially barren and artificial, and shades into deception or other forms of criminal behaviour; or if it attempts to ensure that the cupboard will be bare for the Revenue if an associated avoidance scheme fails; or if it involves a dubious proposition, the only attraction of which is that the "Department will never pick it up": the technical advice must go no further than the legalities, the consequences, and the potential penalties. Nothing said must be capable of bearing the construction that the adviser is endorsing the scheme, or showing how it could be done, or done more effectively. And clearly it will avail the adviser nothing to piously counsel against the scheme and then to draw up the documents or prepare the necessary accounts!

If the adviser confines his technical advice in this way, he is not straying from the ordinary and proper province of a professional adviser, and cannot properly be subjected to criticism.

But in this situation the need for counsel against the scheme is even greater than in the case of the contrived tax avoidance scheme. That need is greater for two reasons. First, to keep the client out of trouble. Secondly, to keep the adviser out of trouble.

In this latter connection, the wise adviser will deliver to his client a written record of his unequivocal advice against proceeding with the scheme. The reason for taking this course has become disquietingly plain to tax advisers in Australia, and very recent utterances of the Under-Secretary for Finance indicate that New Zealand advisers need to become well aware of it if they have not already done so.

That reason is the existence of the crime of conspiracy to defraud the Revenue.

Conspiracy to defraud the Revenue

Crimes Act 1961 s 257 enacts that

> Everyone is liable to imprisonment for a term not exceeding 5 years who conspires with any other person by deceit or falsehood or other fraudulent means to defraud . . . any person . . . :

"person," by s 2(1), being so defined as to "include the Crown".

In the Revenue context the Commissioner is the Crown (*Cates v CIR* [1982] 1 NZLR 530, 534, lines 23-38 per McMullin J; 535, lines 21-25 per Somers J (CA)), and the relevant intent is an intent dishonestly

> to get out of the Revenue something that was already in it, or to prevent something from getting into the Revenue which the Revenue was entitled to get. (*Parker v Churchill* (1986) 65 ALL 107, 121, lines 1-3 per Jackson J (Fed Ct of Aust, Full Ct))

This is essentially a codified common law offence (cf *R v Kidman* (1915) 20 CLR 425, 437 per Griffith CJ (Full High Court)). It is one so serious in its implications, and in its consequences, for it not to be any laughing matter. Of all the cases, only *R v Starling* (1665) 1 Sid 174; 82 ER 1039 seems to have amusement value. First, because the report is in law French. Secondly, because it tells of a conspiracy entered into, by an Alderman of London and 16 other brewers, to "depauperate les fermors del excise": to impoverish the excise men and make them unable to pay the King his due. The agreed means was to be that the brewers would combine for a time to make no more small beer, such as was sold to the poor, and thereby would incite the poor to rise up against the excise men, pull down the excise house, and make their continued functioning impossible.

To find conspiracy to defraud the Revenue it is not necessary that the Revenue actually be presently entitled to be paid tax. Even an entitlement which *might* come into existence, depending on the success or failure of a tax mitigation plan, will suffice: if the object of the agreement is to make that entitlement worthless.

> [I]t is clearly the law that an agreement by two or more by dishonesty to deprive a person of something which is his or to which he is or would or *might be* entitled and an agreement by two or more by dishonesty to injure some proprietary right of his, suffices to constitute the offence of conspiracy to defraud. (*Scott v Metropolitan Police Commissioner* [1975] AC 819, 840F per Viscount Dilhorne (HL, E). My emphasis.)

The relationship between tax minimisation schemes and such conspiracy

Carrying out a plan for tax mitigation of itself can involve no criminal liability under existing enactments.

Speaking in the context of company charges, not Revenue matters, in *Re George Inglefield Ltd* [1933] Ch 1, Romer LJ, in the English Court of Appeal, stated what is nonetheless the general principle:

> If a man so conducts his affairs that he places himself outside the operation of an Act of Parliament, he cannot be said to be either evading it or defeating it. He has done nothing that is unlawful, and he has done nothing that calls for adverse comment from the Court. (Ibid 26)

If the intent behind a scheme (as judged by the acts by which it has been implemented: *Stephens v Abrahams* (1902) 27 VLR 753, 768 (Supreme Court of Victoria, Hodges J)) is nothing more than that income tax will not be payable as a result of it, there can be no question of an offence against the Revenue, even if the scheme ultimately be held to have been ineffective as having infringed Income Tax Act 1976, s 99 or some other anti-avoidance enactment; or even if it be held to fail for some other technical reason, such as inability to satisfy the common law or statutory requirements for validity of a particular transaction or component thereof.

If not only the intent of a scheme, but also its achievement, is the lawful reduction of tax liability, it cannot be a fraud on the Revenue that it also involved the savings being placed outside the jurisdiction, or otherwise made irrecoverable by the Commissioner should he — before the scheme has been judicially upheld — decide to make, and attempt to enforce, an incorrectly based assessment.

In *Vereker et al v Rodda et anor; Forsyth v Same* (Federal Court of Australia, Victoria District Registry, VG 296/1986, 297/1986: decision of Jackson J dated 1 April 1987), the appellants, including a QC, had been committed for trial by a Magistrate on charges of conspiracy to defraud the Revenue. Although the learned Magistrate did not rule on whether the relevant scheme had been effective or ineffective to reduce taxable income to nil, he had considered that a provision akin to Income Tax Act 1976, s 34(2)(b) — permitting tax to be recovered notwithstanding the lodgment of an objection or the pendency of case stated proceedings — gave rise to "interim rights". (judgment pp 22-23). The Magistrate considered that the Revenue had been defrauded of these by aspects of the scheme which ensured that the companies involved in it ended up lacking any funds to pay the tax assessed. (Judgment p 9)

Jackson J, reviewing the Magistrate's decision, would have none of this; discerning

> an underlying fallacy in the view that the "interim" rights are rights of the nature to which Viscount Dilhorne referred [in the passage cited at page 5 *ante*]. It was said on behalf of the second respondent [apparently the police officer who was the informant] that the rights are of the relevant kind but that the real question is whether the Commissioner's ability to recover would be taken away "dishonestly" if the agreement were implemented. I have difficulty with this argument, however, because if what has been done has been to create a situation where a deduction has been lawfully brought into existence reducing taxable income to nil, it is impossible to regard it as dishonest not to keep available the funds necessary to pay an assessment based on the assumption that the deduction claimed will be wrongly disallowed. (Judgment 23-24)

But the position may be to the contrary if there shall have been added to a "chancy" tax mitigation scheme any additional refinement intended to ensure that, should it fail, the tax liability then to arise would be that of a person outside the jurisdiction (cf *Barton v Deputy FCT* (1974) 131 CLR 370, 374 per Stephen J (Full High Ct)), or of a person lacking sufficient means to pay it. (cf *Reg v Hall* (1858) 1 F & F 33; 175 ER 613; *Peter Buchanan Ltd and Macharg v McVey* [1955] AC 516n, 534-535)

The position will be to the contrary where the intent is, by sham or red herring, to conceal from the Commissioner a liability to pay tax. For example, by falsification of primary documents (*Stephens v Abrahams* (1902) 27 VLR 753 (Supreme Court of Victoria, Hodges J), or of the accounts (*R v Harz* [1967] 1 AC 760 (CCA))

Moments at which conspiracy becomes complete and becomes completed

For a reason which I hope shortly will become obvious, it can be important to identify when a conspiracy is formed and when it is spent.

For example, where it has been formed — become complete — outside the jurisdiction, the question can arise whether acts done within the jurisdiction, in furtherance of the object, are triable as conspiracy.

The offence itself certainly is complete once the agreement has been made, and it matters not that no steps may have been taken thereafter to implement the object of the conspiracy: *Reg v Cuthbertson* [1981] AC 470, 481B per Lord Diplock (HL, E).

However it was emphasised by the House of Lords in *Reg v Doot* [1973] AC 807 that the offence continues to be committed by the parties for so long as the agreement remains afoot.

Lord Pearson held, for example, that:

> A conspiracy involves an agreement expressed or implied. A conspiratorial agreement is not a contract, not legally binding, because it is unlawful. But as an agreement it has its three stages, namely (1) making or formation (2) performance or implementation (3) discharge or termination. When the conspiratorial agreement has been made, the offence of conspiracy is complete, it has been committed, and the conspirators can be prosecuted even though no performance has taken place: *Reg v Aspinall* 2 QBD 48 per Brett JA at pp 58-59. But the fact that the offence of

> conspiracy is complete at that stage does not mean that the conspiratorial agreement is finished with. It is not dead. If it is being performed, it is very much alive. So long as the performance continues, it is operating, it is being carried out by the conspirators, and it is governing or at any rate influencing their conduct. The conspiratorial agreement continues in operation and therefore in existence until it is discharged (terminated) by completion of its performance or by abandonment or frustration or however it may be. (Ibid 827B-E)

Viscount Dilhorne was of a like mind, holding that

> though the offence of conspiracy is complete when the agreement to do the unlawful act is made and it is not necessary for the prosecution to do more than prove the making of such an agreement, a conspiracy does not end with the making of the agreement. It continues so long as the parties to the agreement intend to carry it out. It may be joined by others, some may leave it. Proof of acts done by the accused in this country may suffice to prove that there was at the time of those acts a conspiracy in existence in this country to which they were parties and, if that is proved, then the charge of conspiracy is within the jurisdiction of the English Courts, even though the initial agreement was made outside the jurisdiction. (Ibid 825B-C)

For these reasons, the fact that a conspiracy to defraud the New Zealand Revenue becomes complete overseas – say in the Cook Islands – does not rule out the prosecution for conspiracy of additional persons subsequently becoming parties to it in New Zealand.

Accessory roles: inciting, counselling, or abetting

The fact that the conspiracy may be already complete when he is consulted, will not protect an adviser, who fails to confine and qualify his advice, from becoming an accessory, and, therefore, a party to the conspiracy.

Thus, in *Vereker et al v Rodda et anor; Forsyth v Same* (supra), Jackson J held:

> It follows in my view that there may be offences under [a provision resembling Crimes Act 1961 s 61(1)] brought about by inciting, urging, aiding or encouraging others to conspire in terms of [a provision corresponding to Crimes Act 1971 s 257] although the agreement the subject of the conspiracy has been entered into at a time prior to events alleged to attract [s 61(1)]. It is possible, of course, that some parts of [s 61(1)] will be inappropriate to the facts of particular cases, and perhaps of this case, but the issue was argued before me on the broad basis that [s 61(1)] could not be applicable to conspiracy cases and I think I need do no more than reject that broad proposition. (Judgment 30-31)

In relation to conspiracy, the accessory provision is Crimes Act 1961 s 66(1), which enacts that

> Everyone is a party to and guilty of an offence who –
> (a) Actually commits the offence; or
> (b) Does or omits an act for the purpose of aiding any person to commit the offence; or
> (c) Abets any person in the commission of the offence; or
> (d) Incites, counsels, or procures any person to commit the offence.

Advising on how a crooked scheme may be carried out, or improved; preparing accounts or returns designed to effectuate the client's intention to throw sand in the eyes of the Commissioner; preparing documentation for a complex and fraudulent scheme; or backdating documents, including deeds, minutes, memoranda: all are examples. So, even, is preparing such a simple everyday document as a common agreement for sale and purchase, in which the respective values attributed to the land and to chattels or trading stock are to be manipulated in such a way as to raise questions to which the adviser deliberately turns a blind eye.

> If a person is unaware of the essential matters constituting the offence because he has shut his eyes to the obvious, or because he has refrained from making an inquiry which he realised he ought to have made, he may still be convicted of aiding and abetting the offence. (*Halsbury's Laws of England* 4 ed Vol 11 para 45 note 2)

The blindness must be wilful, not merely the result of negligence (:cf *Giorgianni v The Queen* (1985) 156 CLR 473, 488 per Gibbs CJ (Full High Ct)).

Duty not to act over and above one's duty as a solicitor or other adviser

The New South Wales Court of Appeal made some observations in *R v Tighe and Maher* (1926) 26 SR (NSW) 94, which bear repeating in this context:

> It is expected of course of every solicitor that he shall act up to proper standards of conduct, that he shall give his clients sound advice to the best of his ability, and that he shall refrain from doing anything likely to mislead a Court of Justice; but, in the course of his practice he may be called upon to advise and to act for all manner of clients, good, bad or indifferent, honest or dishonest, and he is not called upon to sit in judgment beforehand upon his client's conduct, nor because he does his best for him as a solicitor within proper limits, is he to be charged with being associated with him in any improper way. In acting for a client, a solicitor is necessarily associated with him, and is compelled to some extent to appear as if acting in combination with him. So he may be, but combination is one thing and improper combination, amounting to a conspiracy to commit a crime or a civil wrong, is another thing. An uninstructed jury may easily fail to draw the necessary distinction between such combined action as may properly and necessarily be involved in the relation of solicitor and client, and such

> acts on the part of a solicitor, over and above what is required of him by his duty as a solicitor, as may properly give rise to an inference of an improper combination. I think, therefore, that it may be useful to point out the importance, in cases where a solicitor is charged with entering into an agreement with his client which amounts to a criminal conspiracy, of seeing that the jury are properly instructed as to a solicitor's duty to his client, and that it is made plain to them that, before a solicitor can be convicted of conspiring with his client to commit a wrong, it must be proved that he did things in combination with him, over and above what his duty as a solicitor required of him, which lead irresistibly and conclusively to an inference of guilt. (Ibid 108-109)

In *Vereker et al v Rodda et anor; Forsyth v Same* (supra), Jackson J held these remarks to be "equally apposite to the position of a barrister". (Judgment p 26) They would seem, also, to cover the accountant giving tax advice.

The barrister involved in that case is the leading Melbourne tax silk, Mr N H M Forsyth QC. He was asked to advise on the validity of a company profit-stripping scheme, involving dealing in objects d'art with a public art gallery at grossly inflated prices.

In a written advice he considered the scheme and expressed the view that it would be fiscally effective in the light of judicial attitudes then prevailing. He qualified his advice by noting the artificiality of the proposed scheme, and by warning that, to proceed would involve the usual risks that his opinion would be proven wrong, or that there would be a judicial reaction against artificial schemes.

Following receipt of that advice the scheme promoter launched into it on such a scale that, by the time the Revenue re-assessed to disallow the deductions, about $A30 million of extra income tax was being claimed from the participant companies.

Trouble arose because the effect of the scheme had been to leave the companies stripped of any means to pay the tax.

The participants in the scheme were charged with conspiracy to defraud the Revenue. On the strength of his advice, Mr Forsyth QC was charged with having incited and aided them so to conspire.

A magistrate committed him for trial, but Jackson J, in the Federal Court, remitted the matter for reconsideration by the learned magistrate on all the evidence: remarking, however, that, on such of the evidence as had been placed before him, the learned Judge could see much to support the view that Mr Forsyth had done no more than act as a barrister.

Since one cannot imagine that, on the Review Application, the Crown would have failed to mention any evidence against Mr Forsyth QC, this finding effectively appears to be a direction that the Magistrate rescind his finding.

It seems regrettable that counsel's advice, as reported in the reasons for judgment, ever could have put him in the situation of facing a conspiracy charge.

But, for all tax advisers except Mr Forsyth QC, the prosecution decision to lay the charges may have been a happy one: insofar as it has resulted in a warning to them of how far they may go in advising clients; and has resulted in a warning to the Crown that such charges are not to be made against a tax advisor who has done no more than advise his client in accordance with his professional duty and within the bounds of the "proper standards of conduct."

"Proper standards of conduct" for a tax adviser

In the passage cited at pp 10-11 *ante* from the reasons for allowing the appeal in *R v Tighe and Maher* (supra), the New South Wales Court of Appeal placed first, in its list of the things to be done or avoided by the tax lawyer giving advice, the obligation to "act up to proper standards of conduct".

The adviser as promoter

Obviously, if the adviser is in the position of overtly promoting a scheme which defeats the valid claims of the Revenue; or if his reward is a "slice of the action", or participation in the savings, rather than an ordinary professional fee: there is a great danger of his being found to have gone "over and above what his duty as a solicitor required of him" in a way that leads "irresistibly and conclusively to an inference of guilt" (*R v Tighe and Maher* (supra).

The reason has nothing to do with whether tax avoidance is legal or moral. It is simply that the adviser must cease to advise once his position admits any possibility of conflict between his personal commercial interests and his duty to his client. The considerations were canvassed by Sir Gerard Brennan, when, as a member of the Full Court of the Federal Court of Australia in *Leary v FCT* (supra), he said this:

> [The differences between the roles of professional adviser and of entrepreneur] arise because the field of professional activity is co-extensive with a lawyer's professional duty. That duty is to give advice as to the meaning and operation of the law and to render proper professional assistance in furtherance of a client's interests within the terms of the client's retainer. It is a duty which is cast upon a lawyer, as a member of an independent profession, whether his services are sought with respect to the operation of taxing statutes, the provisions of a contract, charges under the criminal law or any other of the varied fields of professional concern. It is a duty which arises out of the relationship of lawyer and client. But activities of an entrepreneur in the promotion of a scheme in which taxpayers will be encouraged to participate fall outside the field of professional activity; those activities are not pursued in discharge of some antecedent professional duty. Entrepreneurial activity does not attract the same privilege nor the same protection as professional activity; and the promotion of a scheme in which particular clients may be advised to participate is pregnant with the possibility of conflict of entrepreneurial interest with professional duty. (Ibid 434-435)

If the scheme is one coloured by

continued on p 360

Correspondence

Dear Sir,

Re: Pacific Islands Law Officers Meeting: Rarotonga August 1987

In the *New Zealand Law Journal* issue of October reference was made to the "surprising absence from the PILOM meeting of any representative of the New Zealand Law Officers".

Since it is plain that that absence can be and perhaps has been misunderstood, I should place on record that inquiries have been made and, whilst we understand that invitations to attend were sent to us, neither the Attorney-General nor I received one. If we had, it seems very likely that attendance at the meeting would have been arranged.

D P Neazor
Solicitor-General

Dear Sir,

Re: Local Authorities and the Illegal Contracts Act

There is a difference between a contractual provision that is illegal and one that is void on some other ground. A clog on an equity of redemption for example is void but not illegal. The Illegal Contracts Act 1970 s 7 empowers the Court to validate contracts that are illegal *stricto sensu* but confers no power to validate contracts void or unenforceable on any other basis.

An agreement by a local authority to pay a retirement gratuity is *ultra vires* and void unless such a gratuity falls within certain limits set by the Finance Act No 2 1941 s 6(2). In *Lower Hutt City Council v Martin* (noted at [1987] BCL 257 and commented on at length by Mr Beck at [1987] NZLJ 274) the local authority had contracted to pay a gratuity on terms outside the statutory authorisation. The argument on this part of the case both in the District Court and before Heron J seems to have assumed that this was an illegal contract and to have been confined to the question of whether s 7 relief should or should not be granted. Heron J as a matter of discretion declined relief, but was not the short answer to the claim for relief that this was not in any precise sense an illegal contract at all, so that the s 7 jurisdiction never arose?

D F Dugdale

Recent Admissions

Barristers and Solicitors

Anderson KJ	Wellington	15 October 1987	Ikiua PAD	Wellington	15 October 1987
Bradford GNE	Wellington	15 October 1987	Ironside SM	Wellington	15 October 1987
Brewer AJ	Wellington	15 October 1987	Kettle CD	Wellington	15 October 1987
Bridges CJ	Wellington	15 October 1987	Lowe FM	Wellington	15 October 1987
Bridges TJ	Wellington	15 October 1987	Milne JR	Wellington	15 October 1987
Cardinal DB	Wellington	15 October 1987	Narev ED	Wellington	15 October 1987
Carrington PF	Wellington	15 October 1987	Olsen LJ	Wellington	15 October 1987
Catt ML	Wellington	15 October 1987	Postelnik Y	Wellington	15 October 1987
Crengle DL	Wellington	15 October 1987	Powell LG	Wellington	15 October 1987
Davison AP	Wellington	15 October 1987	Ryan SA	Wellington	15 October 1987
Diamond EJ	Wellington	15 October 1987	Scott RJ	Wellington	15 October 1987
Dougal AR	Wellington	15 October 1987	Shera RJ	Wellington	15 October 1987
Elliott PR	Wellington	15 October 1987	Skinner KM	Wellington	15 October 1987
Hart AM	Wellington	15 October 1987	Stevens RB	Wellington	15 October 1987
Heimsath J	Wellington	15 October 1987	Symonds MR	Wellington	15 October 1987
Howes GR	Wellington	15 October 1987	Weston TS	Wellington	15 October 1987

The financial structure of a partnership

By Murray Landis and Attila Kameron of Sydney, Australia

The authors are a solicitor in the firm of Moore and Bevins, and an accountant in the firm of Touche Ross and Co in Sydney. In this article they consider the cash and funding aspects of professional partnerships. An earlier article by one of the authors, Murray Landis, on profit sharing was published at [1987] NZLJ 8.

1 Introduction

The challenge for professional firms in the years ahead will be to balance three competing cash demands – finance for the business, Partners' lifestyle and the taxman. This article examines the various demands and options available to satisfy them. We look at how Partnerships work from a financial viewpoint and in particular, how they are funded. We also consider some traditional Partnership structures and suggest a number of new approaches.

Typical questions that Partners are seeking answers to are:

1 How should the firm's finances be structured so as to maximise profit to Partners?
2 What level of Partner draws is desirable and possible?
3 What should the gearing (external borrowings : retained earnings) of the firm be?
4 What credit facilities are offered by banks today?
5 What is the value of the firm and individual Partners' shares?

Many firms fund themselves almost entirely out of Partners' capital and withheld earnings. Sometimes this is not the result of a conscious planning decision, but simply that Partners have regularly, over a long period drawn less in cash than their taxable share of profits. These accumulated draws left in the firm provide the funds used to meet external expenses and liabilities and also practice expansion. New Partner entry into these kinds of firms is typically very expensive involving a sizeable capital investment, often called "goodwill". However, even these firms are now rethinking this approach since they need to attract high-calibre Partners in a different financial environment to 100 years ago or even 10 years ago. The average aspirant to Partnership in a professional firm today is asset-poor and has limited capacity to make a major capital investment.

On the other hand, older and more senior partners are not prepared to carry the capital burden disproportionately, particularly when the incomes of Partners are levelling. At the same time the retirement of these older Partners can make a big hole in Partnership Funds when they are paid their disproportionate share of capital.

With careful Partnership financial planning and management, it is possible to find a balance between the needs of the firm and those of Partners, both old and young.

2 Key Terms

Gross Fees

The taxable income of most professional firms is calculated on an earnings rather than a cash basis. Gross Fees (or earnings) are the actual fees billed to clients during the financial year.

Work in Progress (WIP)

This is the value of work undertaken for clients that has not as yet been billed. In most Partnerships, depending on the average duration of assignments and the relationship with clients, WIP typically amounts to the value of two to three months' work. In some firms, WIP may correspond to as much as nine or even 12 months' work. This invariably occurs where there is no regular or progressive billing until matters in hand are completed. As we will see, this is a very costly practice.

Debtors

Clients with outstanding accounts, as well as the value of accounts rendered but not yet paid, are both referred to as "Debtors".

Professional firms mostly render accounts net 30 days and are paid within 60 days.

Billable work generated

In a Partnership, billable work is undertaken on a daily basis. In some firms this work is recorded on a task or scale basis and in others it is recorded on a time basis.

Partnership expenses

This includes all expenses associated with operating the firm: salaries,

premises costs, equipment and so forth, but excludes the income of Partners who receive a share of profits.

Drawings
Partners take their share of income as cash distributions or payments out of firm profits (calculated as Gross Fees less Partnership Expenses).

Partnership Retained Earnings
Partnership Retained Earnings is the cash that is withheld from Partners in order to finance the firm's WIP and Debtors. In practice, Partners Drawings are delayed until sufficient cash is available for them to be paid.

Partnership Capital
Another method of financing the firm is for Partners to inject capital. The Partner may make this investment by cash payment on joining, or over a period of time. Alternatively, part of the Partner's Share of Partnership Retained Earnings may be converted to capital.

External Funding
Apart from Partnership Retained Earnings, working capital is usually provided by means of bank Overdraft accommodation, Fully Drawn Advances, Term Loan, Bill Lines and other Financing Facilities. Finance is also obtained for the purchase or lease of office equipment and furniture.

Gearing
This is the ratio of external debt to Partnership capital and retained earnings. Typical ratios are in the range 30:70 to 70:30.

3 How a Partnership works from a financial viewpoint

Let us look now at how the finances of a Partnership work.

Billable work is undertaken by Partners, managers and support personnel on a continuing basis. Fees are rendered for this work several months later. There is a further delay until cash is received from clients in payment.

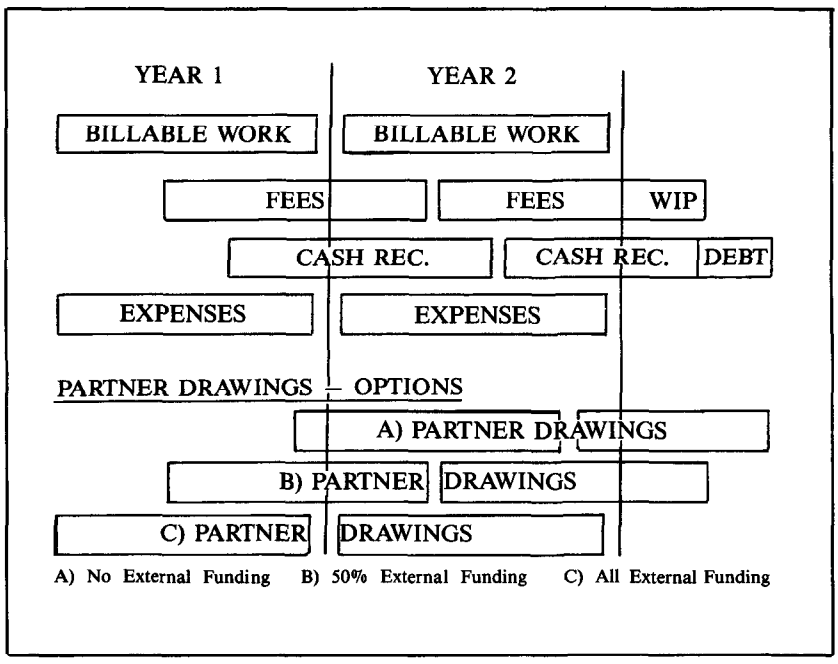
Firm expenses, on the other hand, such as salaries, rent and other operating overheads, are normally paid at about the same time that the billable work is done.

The difference in timing between receipt of cash and payment of expenses results in a need for substantial funding to support the Partnership. For most well-run firms, Partnership profit in any year is about the same or a little less than the value of WIP plus Debtors. However, WIP and Debtors are uncollected amounts and only the excess of cash received over expenses paid is available for distribution in the absence of external funding. Profit can be drawn from the previous year's work, since the cash represented by WIP and Debtors for that year will have been collected.

If the time lag between doing work and getting paid is too long, not only is there an excessive financing cost, but in effect Partners are drawing income out of profits from work that in some cases may have been undertaken up to two years previously. The cash received will be based on charge rates prevailing at the time the work was undertaken, not current rates. Those inflation devalued dollars will need to be used to meet today's commitments. A further consideration with excessive WIP is the increasing risk of the amounts becoming uncollectable.

The effects described above can be illustrated by the following simple example:

This effect is illustrated clearly in the diagram below.



Partnership Cash Flow – What Happens

EXAMPLE — Loot & Divide is a Four Partner Firm with $1.2M Annual Fees

The firm undertakes billable work at a steady rate of $100,000 per month.

3.1 Fees Rendered
Loot & Divide manages its affairs fairly well and bills 20% of work done within 30 days, 40% within 60 days and the remaining 40% within 90 days. From the start of business in month 1, the value of fees rendered is as given in Table 1 below.

Table 1: Timing of Fees Rendered versus Billable Work

	Month						Half Year
	1	2	3	4	5	6	Total
Value of Billable Work	100	100	100	100	100	100	600
Less Fees Rendered:							
Month 1 Work	0	20	40	40	0	0	100
Month 2 Work	0	0	20	40	40	0	100
Month 3 Work	0	0	0	20	40	40	100
Month 4 Work	0	0	0	0	20	40	60
Month 5 Work	0	0	0	0	0	20	20
Total	0	20	60	100	100	100	380
Balance of WIP at the end of the period							220

Under this fairly aggressive WIP to Debtors conversion schedule, the average value of outstanding work in progress is $220,000 representing 2.2 months' billable work and 18.3% of annual fees.

3.2 Cash Received

Once fees are rendered, there is a further wait for cash. Loot & Divide's clients are good payers; 30% pay within 30 days, 40% within 60 days and the balance of 30% within 90 days,. The schedule of cash receipts is as set out in Table 2 below.

Table 2: Schedule of Cash Received versus Fees Rendered

	Month						Half Year
	1	2	3	4	5	6	Total
Fees Rendered	0	20	60	100	100	100	380
Less Cash Received:							
Month 2 Fees	0	0	6	8	6	0	20
Month 3 Fees	0	0	0	18	24	18	60
Month 4 Fees	0	0	0	0	30	40	70
Month 5 Fees	0	0	0	0	0	30	30
Total	0	0	6	26	60	88	180
Balance of Debtors at the end of the period							200

* From Month 6 on, the cash received is 100 in each month

Of the $380,000 in fees rendered, $180,000 is collected by the end of the six month period. This means the value of outstanding Debtors at period end is $200,000 representing two months' billable work and 16.7% of annual fees.

The combined total of period end WIP and Debtors in our example is $420,000, representing 4.2 months' work and 35% of annual fees. Hence of the $600,000 in value of work undertaken, only $180,000 is collected as cash within the six month period.

3.3 Expenses and Profit

Whilst cash receipts are delayed, most expenses are incurred in the same time frame as undertaking billable work. Let's say Loot & Divide has a profit rate of 33.3%. That is, expenses on an annual basis (excluding Partner draws) comprise 66.7% of fees. Thus expenses for the six month period are $400,000 and must be paid in the period.

Cash receipts are only $180,000 so there is a cash shortfall of $220,000. At year end, cash received increases to $780,000 ($180,000 + $600,000) with expenses of $800,000 reducing the cash shortfall to $20,000. But this is before partner draws!

3.4 Financing Needs

By the end of the first six months' business, Loot & Divide has a major cash shortage problem. $220,000 is needed to finance the cash shortfall and a further $200,000 to fund Partners' draws (33.3% of $600,000). By the end of the first year, the cash shortfall has been reduced to $20,000, but total cash needed is still $420,000 since $400,000 in Partners' draws must be funded.

This basic cash need of the firm is its working or Partnership funding capital requirement. It can be calculated either as the value of WIP plus Debtors ($220,000 + $200,000) or the cash shortfall plus Partner draws over 12 months ($20,000 + $400,000).

With billable work running at $100,000 per month and a profit rate of 33.3%, an ongoing funding

shortage of $420,000 to enable Partners to fully draw their share of profit will come as a surprise to most Partners. It is a surprise because these Partners would not consider there to be a shortage of $420,000; they would only see the cash shortage to pay ongoing bills and themselves a basic "salary" and would externally fund that amount usually by overdraft accommodation. These Partners recognise the need to fund their basic salary because they have to pay day-to-day living expenses but they ignore the need to fund further Partner draws, preferring to wait until the cash from Debtors is "in the tin". This is a fairly typical situation and in the case of Loot & Divide it would actually take 12.6 months with a monthly profit rate of $33,333, to collect and distribute $420,000 of withheld drawings.

4 Partnership and bank financing

Virtually all Partnerships arrange for firm financing through a combination of external borrowing, the injection of capital by Partners and through Partners delaying drawing of their entitlement to profits.

Loot & Divide realised they had an ongoing funding problem. With no external borrowing, their investment in the WIP and Debtors of the firm would be $420,000 or $105,000 each. The firm decided to borrow 50% of its total funding requirement, ie $210,000 from the bank. This reduced the investment required by Partners to $210,000 which represents 6.3 months' drawings.

Each partner at Loot & Divide decided to contribute $12,500 as capital to establish the firm and they decided that future Partners should pay that amount on joining. This reduced the withheld earnings component from $52,500 each to $40,000 or from 6.3 months to 4.8 months so that the balance of drawings available to be drawn out of current years' earnings corresponds to 7.2 months' profit. The Partners of Loot & Divide also decided they wanted the external funding to stay at that level so they expressed the ratio of their external debt to total funding as a debt to equity or gearing ratio (in this case 50:50) which was then maintained as part of the firm's financial planning. Some of the Partners separately borrowed their $12,500 capital from the bank and obtained a deduction for the interest on that loan.

Loot & Divide were pleasantly surprised when they approached their bank for increased credit facilities. The manager was receptive to their approach and offered generous facilities on good terms.

It is important in looking at your firm to calculate on the *total* Partnership funding requirement. Many firms forget or ignore WIP and therefore believe their gearing is higher than it really is and conversely that their Partners' investment in the firm is lower than it really is. Obviously, the lower the external debt, the greater the amount of the Partnership funding requirement which must come out of Partners' capital and withheld earnings and vice-versa.

In either case there is an interest cost. There is a direct and visible cash outlay in the form of interest expense to the bank when external debt is used. There is no cash outlay for the firm if it is funded by partners' capital or withheld earnings, however the individual Partner pays a real cost. He is earning no interest on the moneys he has "lent back" to the firm. At the same time he may have significant borrowings. Alternatively he may be forgoing an attractive opportunity.

These Partners would be better off having borrowed funds to invest in the firm and freeing their capital for debt reduction on investment.

Whilst higher commercial rates of interest apply for this Partner or Partnership borrowing, the interest payment is a legitimate business expense to finance the working capital of the firm and hence is tax deductible. In today's market, that brings the after-tax cost of borrowing to less than 10%, a substantial reduction on the 15.5% payable on the home mortgage.

5 Partner draws and the effect of growth

In most firms, Partners receive a base level of monthly drawings as a notional salary. Periodically a special draw occurs when there is sufficient cash on hand. It is actually possible for firms to plan and budget for Partners cash drawings. As we have seen the Partners of Loot & Divide in a given year are able to draw cash corresponding to 7.2 months' work from the current year's profits. The remainder of 4.8 months is held within the firm to finance Debtors and WIP for the current year. The 4.8 months' profit held over from the previous year is now able to be distributed this year. If there is no growth in business, the withheld earnings from last year equal the withheld earnings from this year and there will be a 100% draw rate.

Where there is growth in earnings, the earnings withheld this year will be more than those withheld last year so the total cash drawing this year will be less than the Partners' share of current year's profit on which tax is paid. In practice, with growth rates around 20%, and WIP and Debtors' figures as above, Partner drawings this year will be reduced to around 90% of profits.

Both WIP and Debtors increase in direct proportion to the increase in billable work. It is this increase in WIP and Debtors that causes the shortfall in drawings available to Partners. The shortfall in drawings is equal to the amount of the increase. Partners can either fund the increase themselves or it may be funded by a combination of reducing Partner drawings and increasing bank borrowings.

Traditionally, most firms have had low gearing ratios with between 10% and 30% of total Partnership funding coming from external borrowing. It is easy to see how this came about. Since the natural outcome of growth is to reduce gearing, banks have not encouraged firms to borrow and professional firms have been conservative in their financial planning.

Low gearing ratios have a major impact on the lifestyle quality of Partners since growth is then funded disproportionately out of their pockets.

Each firm needs to determine the drawing level it requires in order to meet Partners' living needs and tax. The level of external debt to enable that draw to take place can then be calculated. The higher the level of debt, the faster Partners will get their cash. The lower the level of debt, the longer Partners will have to wait. If a set level of debt : equity

ratio is agreed upon between Partners and the bank, then external funding can quite simply increase from year to year at the desired rate.

6 Value of the Partnership and Partners' share

Traditionally, Partnerships include Debtors as their primary asset on their balance sheet. There are two reasons for doing this:

(a) fees rendered constitute the basis on which taxable income is determined; and

(b) once a bill has been rendered, there is a debt due by the client which can be sued for or transferred so that legal entitlement to payment for the work done has been established.

Without question then, Debtors are an important asset of a Partnership.

However, WIP is also a very important asset. Cash has been expended and liabilities have been incurred in order to create it. Not quite as tangible as Debtors, WIP still represents future income and current accounting treatment indicates it belongs on the balance sheet. The amount of WIP that should be shown on the balance sheet is another question entirely. Just as allowance is made for bad and doubtful debts, so allowance has to be made for WIP which may be written off. The older the average age of WIP, the more difficult it will be to collect. Very old WIP often becomes unbillable, unlikely ever to be collected and carried forward from one year to the next. Bad WIP, like Bad Debts, must be cleaned out at least once a year and certainly at balance date.

Other assets include office facilities, library, plant and equipment which may be owned rather than leased. However, these latter items do not usually amount to a large proportion of total assets and if they do (for example with computer equipment, which may be more tax effective owned than leased) the asset is usually offset by a liability about equal to the written down value.

The effect of external borrowing is to reduce the value of each individual Partner's share in the Partnership and hence also to reduce the cost of entry for new Partners. At the other end it reduces the cost to the continuing Partners of paying out a retired or deceased Partner. Any additional amount that an individual Partner wants or needs for retirement can be more effectively provided by Superannuation.

In our analysis, we have ignored goodwill. In earlier days, "goodwill" was really used as a surrogate for the value of WIP since that item was not treated, and often not regarded, as an asset. With WIP added in to Partnership worth, a very careful analysis needs to be carried out before so called "goodwill" is included as an asset.

7 Conclusion

The thrust of this article has been to focus on the factors which need to be examined to optimise the Partnership's and each Partner's financial position.

Firstly: WIP and Debtors must be kept as low as possible to minimise the cost of financing the firm and to enable Partners to receive their profits in current, not inflation-devalued, dollars.

Secondly: To the extent that the firm and individual Partners need to finance WIP and Debtors, the debt and investment involved ought to be tailored to meet the needs of the firm and its Partners in the most tax effective way.

There is no single or correct financing structure or funding method which is ideal for all firms. The basic principles, however, are of general application. □

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fraud, the promoter will be a prime target for a charge of conspiracy to defraud, and he will be unable to hide behind his professional status because he will have abandoned that status by having adopted the entrepreneurial role.

Where the adviser merely assists a promoter

The same is likely to apply to the professional adviser who promotes someone else's scheme on a commission basis: except that the additional risk will arise of the commission of an offence under the Secret Commissions Act 1910.

Tax advice as a sales aid

Even where the adviser does not promote the other's scheme, but merely is asked to advise that other on it, great caution is required.

If the adviser knows his advice is to be included in a prospectus, it is proper to give his views on the principles applicable to the facts on which he is asked to advise.

However, when one considers how frequently the actual implementation of merchandised schemes is found to vary from the proposed manner of execution, it would be, at best, imprudent were the adviser to fail to make it plain that his advice is being given on the basis that it must be published in full, and to ensure that that full advice makes it clear that it is based on certain factual suppositions which he has been asked to make, and that it will not hold good if those factual suppositions are not made out.

The advice should make clear that the factual suppositions are no more than that; that the adviser is in no way attesting that they will be made out; and that he is in fact cautioning investors to be alert to ensure that they are made good. Most schemes are sold on the basis that the parties will be carrying on a business. So it must also be made clear that if, in fact, no business is found to have been carried on, the conclusions expressed in the advice will not hold good.

Finally, if any of those to whom the scheme has been almost sold approach the adviser for additional advice in connection with their possible participation, it is at least imprudent to act, and it certainly would be improper to do so without pointing out emphatically that the adviser's situation is pregnant with the possibility of conflict between the respective interests of promoter and intended participant. □

Creditors' protection and the share premium account

By M J Ross, Department of Accountancy, University of Auckland

In this article the author discusses the effect of the Companies Amendment Act 1982 on the protection provided for creditors of a company by s 64 of the Companies Act 1955. From an accounting point of view he considers that practices have now developed that effectively enable what should be regarded as capital to be treated as revenue to the detriment of creditors.

The capital maintenance rule in company law contains a trade off. Shareholders are protected against action from unpaid company creditors but the capital of the company is to be kept intact to meet creditors' claims.

An amendment to the Companies Act 1955 has dented this rule and prejudiced creditors.

The 1982 Amendment to the Act allows a share premium arising on a takeover to be recorded as distributable profits. Companies have been quick to exploit this provision.

A share premium arises when shares are issued at a price in excess of their nominal value. Court approval is required to source a cash dividend from the share premium account. Approval is refused if payment will prejudice company creditors. Section 64 of the Companies Act 1955 treats the share premium account as part of the share capital of the company.

Court approval is not required, on the other hand, to source a dividend from reserves arising from undistributed capital or revenue profits. These reserves can be distributed to shareholders on the recommendation of directors and with the approval of shareholders.

The protection for creditors contained in s 64 has been overidden by the 1982 Amendment to the Companies Act.

The 1982 Amendment followed a rash of corporate restructuring earlier this decade.

In 1980, Fletcher Challenge Ltd was created by the merger of Fletcher Holdings Ltd, Challenge Corporation Ltd and Tasman Pulp and Paper Ltd. In 1981, the NZ Insurance Co Ltd and South British Insurance Co Ltd merged to form a new company called NZI Corporation Ltd.

There are a number of different accounting treatments which can be used to account for mergers and takeovers. The accounting treatment used for these two mergers was the "pooling of interests" method. This accounting method was developed in the United States. American corporation law has no equivalent of the New Zealand s 64.

An English tax case, *Shearer v Bercain* [1980] 3 All ER 295, signalled to the accounting profession in New Zealand that the pooling of interest method used by Fletcher Challenge and NZI Corporation was illegal.

The consequence of using the pooling of interests method can be illustrated by using a rough analogy from outside company law.

Presume Doe owns land valued at $200,000. Neighbour Roe owns land valued at $100,000. They agree to merge their respective holdings. The two properties are now owned collectively by Doe and Roe; Doe as to a two-thirds share and Roe to a one-third share. They jointly own the land – the "capital stock" of $300,000.

Now presume Doe had previously purchased the land for $50,000. This land was valued at $200,000 at the time of the merger. Prior to the merger, Doe enjoyed an unrealised profit of $150,000. Presume Roe's land, valued at $100,000, cost $75,000. Roe held an unrealised profit of $25,000.

Doe and Roe separately held unrealised profits totalling $175,000. This profit element was recognised in the terms of their merger and is now included in the $300,000 capital stock of their merged properties.

If Doe and Roe were companies, s 64 of the Companies Act 1955 would prohibit their merged company from distributing any part of this capital in cash without Court consent. It is to be held available to meet the claims of creditors.

If pooling of interests was used to account for the merger of Doe and Roe as companies then their collective pre-acquisition profits of $175,000 would appear as part of shareholders' funds in the balance sheet of their merged company in the guise of a distributable reserve.

The criticism is that to source a cash dividend from this distributable reserve would be a return of part of the purchase price paid. It would be a reduction of capital without Court approval. These profits were taken into account in assessing the "price" paid on the merger of their respective interests.

Following *Shearer v Bercain*, use of the pooling of interests method by Fletcher Challenge and NZI Corporation was validated by a temporary measure, the Finance Act (No 2) 1981. Subsequently, the Companies Act 1955 was amended by the insertion of ss 64A-E.

This Amendment allows the pooling of interests method of accounting where a takeover is achieved by:

- purchasing at least 90% of the shares in the company being acquired, or
- purchasing all its assets.

The Amendment allows the new merged company to record as retained earnings in its balance sheet any premium arising on the shares issued to achieve the takeover. The premium commonly reflects pre-acquisition profits held by the two

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Section 23A of the Evidence Act 1908 and the regulation of sexual history evidence

By Steven J Zindel, a Wellington practitioner

This article treats of the amendment to the Evidence Act 1908 concerning the sexual experience and reputation of complainants. The article is based on research done by the author for his Masters degree at Canterbury University. He concludes that the statute has been reasonably successful and that this is largely due to the consistent approach by the Courts in viewing sexual violation as an exception to fundamental principles of the criminal law and the law of evidence.

Introduction

New Zealand has statutory restrictions on the adducing of evidence or the questioning of the complaint in cases involving sexual violation. They are to be found in s 23A of the Evidence Act 1908, as amended in 1985. The 1985 Amendment to the Act merely substituted references to sexual violation in the place of rape in the previous 1977 Amendment. Thus, regulation in this area has been in place for some ten years and there has now developed a body of case law to provide some guide as to its application. It is submitted that the quite restrictive rules concerning the examination of the complainant's sexual past are interpreted in a common sense way by the Courts that does not work injustice to the interests of the accused and which is consistent with evidential principles in criminal law generally.

The Common Law Position

Prior to reform of the Evidence Act in 1977, there were already significant protections for the rape complainant. These are found in ss 13 and 14 of the Act and effectively cast a duty on the Court to decide whether certain questions relating to the credit of the witness upon cross-examination need to be answered. Imputations against the complainant's character are only required to be brought out where they would have a serious effect on her credibility and that of her evidence, and where the importance of the evidence is sufficient to justify the undermining of the witness's credibility. Indecent or scandalous questions are prohibited by s 14. These protections reflect those available at common law but appear to have been applied inconsistently by the Courts. (See the comments of Wells J on the South Australian equivalents in *R v Gun; Ex Parte Stephenson* [1977] 17 SASR 165, 179.)

Clearly, certain evidence relating to the complainant's sexual history is admissible where it is relevant to a fact in issue such as whether the accused had intercourse with the complainant at all. Where consent is in issue, as it usually is, the common law regarded as relevant, evidence of the complainant's general sexual reputation and moral character (*R v Clarke* [1817] 171 ER 633) and her sexual relations with the accused on occasions other than that in issue at trial.[1] The complainant's sexual relations with persons other than the accused was subject to statutory *caveat*, allowed to be admitted. (*R v Bashir* [1969] 3 All ER 692, 693; *R v Holmes* [1871] 12 Cox CC 137) So, in accordance with the general principle that a party may not call witnesses to contradict an opponent's witness on a matter going only to credibility, the complainant's answers to questions on cross-examination could not be rebutted.

The distinctions are easy to state but there was considerable overlap in implementation. While evidence of intercourse with persons other than the accused was generally regarded as going only to credit, an exception was acknowledged at common law where it was alleged that the complainant was a prostitute (*R v Bashir* supra; *R v Clay* [1851] 5 Cox CC 146) or perhaps merely promiscuous.[2] This appears to tie in with evidence of moral character and sexual reputation being admissible on the issue of consent, as well as that of credibility.

In a manner not inconsistent with the rest of criminal law,[3] similar fact evidence in favour of the accused was allowed to be adduced. Where the other acts of the complainant were sufficiently connected with the event in question, either in time, place or other circumstances[4] they could be relevant to the issue of consent in that the complainant might be more likely to consent or the accused may have believed that this was the case.

Issues and credit

The distinction between evidence relevant to issues and that relating to credit is somewhat misleading in that evidence truly affecting the reliability of evidence given by a witness will indirectly be relevant, that is it will affect the probability of the existence of facts in issue. (*R v Kilbourne* [1973] AC 729, 756) However, the view that a "loose woman" is intrinsically unreliable seems now to be universally discredited. (See for example, *R v Gun; Ex p Stephenson* [1977] 17 SASR 165, 168, 174, 185.)

Allegations as to the sexual history of the complainant were not considered as involving common

law "imputations" against her, for the purposes of any retaliatory adducing of character evidence and previous criminal convictions of the accused by the prosecution. In *R v Turner* ([1944] KB 463. Approved in *R v Selvey* [1970] AC 304) it was conceded by Humpries J that to suggest that a woman would have sexual intercourse even with a man not her husband would, to most people, be considered an imputation on her character, but in a rape case it was no more than to call the complainant a liar. (To accuse a Crown witness of lying is not regarded as casting an imputation on character: *R v Rouse* [1904] 1 KB 184.) Provided the accused did not go out of his way to make an attack on the complaint founded upon matters outside the "pith and substance of the charge" (Per Jelf J in *R v Sheean* 24 Times LR 459) the accused did not lose his shield. (See section 5(2)(d) of the Evidence Act which is essentially governed by these rules based on section 1(f) of the Criminal Evidence Act 1898 (UK): *R v Clark* [1953] NZLR 823.)

The Perceived Need for Reform:

In the light of changing social attitudes towards sexual behaviour, it has become accepted that many of the common law assumptions as to sexual experience affecting the likelihood of consent to particular intercourse with the accused or as indicating the complainant's veracity are without foundation. An ill-defined and not very clearly isolated pattern of sexual activity had been overstated by the law as forming the basis for an inference of consent on the part of the complaint in a separate occasion and led, to some extent, to the complainant being on trial. Acquittal of the accused implied that the complainant had made up her allegations and what she had to endure then served to discourage other victims from reporting sexual attacks. While there may be many causes of an initial failure to report sexual violation, such as family and peer pressure, fear of retaliation, not wishing to implicate the attacker and feelings of guilt, the stress of giving evidence at trial for a perhaps 50-50 chance of conviction[5] seems to play a large part. This is illustrated arguably, by the fact that 63.5% of reported rape offences were "cleared" as "no offence" in the year ended March 1986. (Police Report to Parliament)

All this was seen as inhibiting the desirable criminal law policy of prosecuting the guilty, as well as the protection of witnesses and the maintenance of their sexual privacy. (See generally S Odgers [1986] 11 Syd LR 73.) The law relating to the admission of sexual history evidence appeared to need tightening up.

Against this, were the arguments that our criminal law system has as its centrepiece the ideal of justice for the defendant, above all, and whatever the ordeal required in submitting to personal and intrusive questions about one's sexual past, that was outweighed by the torment of an innocent but convicted sexual offender in prison. Further it was argued that sexual violating was not only a "special" offence because of the personal involvement of the alleged victim, but also because rape was an allegation easy to make but harder to deny. Often, the disputed incident occurs with none present save the participants and it may be the case that the opportunity to lie with impunity is greater than with other trials. The interrogation of the alleged victim could also be seen to be more intense, however, detracting somewhat from any motivation to lie.

While it may be disputed therefore that unfounded allegations are a factor in sexual offences more than any other crimes, the same requirements of ensuring a fair trial for the accused are present. To prevent the defence from putting all the relevant evidence before the jury is not to give the accused the fairness our criminal system regards as necessary. The general perception was, however, that the admission of sexual history evidence needed to be regulated. The Courts were not seen as having taken it upon themselves to ensure that evidence of only tenuous but intrusive relevance was excluded and the legitimate demands of prosecution appeared not to be fulfilled. But, at the same time, crimes of sexual violation were inevitably serious, carrying far-reaching ramifications for the accused, and controls on the introduction of evidence could not be too inflexible. The debate was chiefly concerned with the type of regulation to be implemented and when the time came New Zealand opted for a more rigid rule-based reform.

The Practical Operation of Section 23A

In 1977, the Evidence Act 1908 was amended by the insertion of s 23A restricting the admission of certain evidence relating to the complainant's sexual history for offences of rape. As a result of the widening of the law to make rape but one aspect of sexual violation in the Crimes Act, a new s 23A was inserted by the Evidence Amendment Act (No 2) 1985. The rules themselves have not been altered but merely extended in application from the 1977 Reforms. The relevant provisions are as follows:

Section 23A (2). In any case involving sexual violation, no evidence shall be given, and no question shall be put to a witness, relating directly or indirectly to—

(a) The sexual experience of the complainant with any person other than the accused; or
(b) The reputation of the complainant in sexual matters,

— except by leave of the Judge.

Section 23A (3). The Judge shall not grant leave under subsection (2) of this section unless the Judge is satisfied that the evidence to be given or the question to be put is of such direct relevance to:

(a) Facts in issue in the proceeding; or
(b) The issue of the appropriate sentence, — as the case may require that to exclude it would be contrary to the interests of justice:

Provided that any such evidence or question shall not be regarded as being of such direct relevance by reason only of any inference it may raise as to the general disposition or propensity of the complainant in sexual matters.

Section 23A(4). Notwithstanding subsection (2) of this section, leave shall not be required —

(a) To the giving of evidence or the putting of a question for the purpose of contradicting or rebutting evidence given by any witness or given by any witness in answer to a question, relating directly or indirectly, in either

case, to,–

(i) The sexual experience of the complainant with any person other than the accused; or
(ii) The reputation of the complainant in sexual matters; or

(b) Where the accused is charged as a party and cannot be convicted unless it is shown that a person other than the accused committed an offence [of sexual violation] against the complainant to the giving of evidence or the putting of a question relating directly or indirectly to the sexual experience of the complainant with that other person.

Section 23A(5). An application for leave under subsection (2) of this section –

(a) May be made from time to time, whether before or after the commencement of the proceeding; and
(b) If made in the course of a proceeding before a jury, shall be made and dealt with in the absence of the jury; and
(c) If the accused or the accused's counsel so requests, shall be made and dealt with in the absence of the complainant.

Section 23A (6). Nothing in this section shall authorise evidence to be given or questions to be put that could not be given or put apart from this section.

The rather restrictive approach adopted by Parliament can be seen in a number of ways. A prohibition has been placed on evidence or questions as to the sexual experience of the complainant with any person other than the accused and as to her general sexual reputation. The only grounds allowable for the Judge to dispense with the prohibition is that the evidence or questions are of "direct relevance" to facts in issue or the appropriate sentence, to the point that exclusion would be contrary to the interests of justice. Evidence relevant solely as to credit, if that is possible, is not admissible. The rather imprecise test of "direct relevance" may not be satisfied by propensity reasoning of the kind based on Lord Herschell's first prohibitive limb in *Makin v AG* [1894] AC 57, 65 for similar fact evidence against the accused. The problem with this is that, as their Lordships in *R v Boardman* [1975] AC 430 appear to accept, evidence which is sufficiently relevant may be admissible notwithstanding breach of the inadmissible chain of reasoning. (See Hoffmann 91 LQR 193) It is the statutory test in s 23A(3) which might arguably be the determinant of the level of relevance required to surmount the proviso but it is expressly excluded if the relevance rests solely on propensity reasoning. Perhaps it is right to draw the distinction as Lord Hailsham does in *Boardman* [1975] AC 430, 453 between "a chain of reasoning" and "a state of facts" and that for s 23A(3) if the evidence has the necessary direct relevance then it has relevance independent of propensity reasoning. However, all this rather seems to split hairs.

Considerations of policy

It might be argued that it is not the statutory test of "direct relevance/interests of justice" which overrides propensity reasoning but considerations of policy à la *Boardman* [1975] AC 430 when the prejudicial effect of such evidence is outweighed by its probative value. But this is an accused-orientated doctrine not traditionally a victim-orientated one. Further, if other considerations of policy may be divined at all, they will either be identical with those of the statutory test or will have no operation at all, so enabling the accused to cast a reasonable doubt on the prosecution case. Only the twin extremist poles remain, either the propensity reasoning proviso in s 23A(3) has no effect or it must be given effect to override any common law considerations of overwhelming relevance. It is submitted that those responsible for drafting s 23A were overly influenced by the discursive form of common law reasoning as to similar fact and neglected the fundamental principles of relevance which are mandatory in this field.

No restrictions are placed on the sexual experience of the complainant with the accused, save that it bears on the general sexual reputation of the complainant. Reputation is a rather amorphous concept and it might be wondered whether it is not totally irrelevant to the question of whether the complainant did or did not consent. The reality behind the reputation should be the important consideration. On the other hand, the accused's *knowledge* of the complainant's reputation might indeed be relevant to whether he believed she was consenting. It could even go to show the now necessary reasonable grounds for belief.

Also not excluded is rebuttal evidence concerning the sexual experience of the complainant with third persons or her reputation. Presumably, this includes evidence of an absence of sexual experience.[6] Naturally, to deny the defence an opportunity to correct any false impressions gained by the jury would be to seriously inhibit the conduct of its case. There is no requirement that the rebuttal evidence should meet the statutory test of relevance in s 23A(3) and presumably common law rules retained by s 23A(6) apply. Further, alleged parties to offences of sexual violating may adduce evidence or question the complainant as to her sexual experience with the principal.

Procedurally, the effect of the regulation is not lost by the jury getting wind of the evidence sought to be restricted. Applications for leave to dispense with the general prohibition under s 23A(2) may be made at any time but if made in the course of a proceeding before a jury shall be made and dealt with in the absence of the jury. If the accused so requests, the complainant need not be present. Perhaps this is to prevent her reaction to the proposed questioning influencing the trial Judge and may also operate to reduce her distress somewhat, if the defence regards this as desirable.

Prohibition of sexual history evidence other than as between the complainant and the accused or in rebuttal is quite general with the only exception being where it is so directly relevant to facts in issue or sentencing that to exclude it would be contrary to the interests of justice. The test of direct relevance was criticised by Wells J in the South Australian case of *R v Gun; Ex Parte Stephenson*[7] as being either unnecessary if it is meant to demarcate evidence relating to credit and that relating to a fact in issue, or as unjustified if intended to distinguish between direct and indirect relevance. His Honour's

criticisms have just as much force here in New Zealand. The test is, however, obviously intended to be strict but this does not seem to have inhibited the Courts from viewing relevance in more flexible terms, allowing even attacks on the complainant's credibility as being directly relevant to facts in issue.[8] It is noteworthy that Cooke P observed in *R v McClintock* (CA 39/86 (unrep)) that:

> in its terms the New Zealand section appears to be possibly more restrictive of the latitude of the defence than any of the sections in force elsewhere, perhaps more semantically than practically.

To view the level of regulation imposed as only "semantically" different from more discretionary reforms seems to prevent the rules from inflicting injustice but indicates, it is submitted, some degree of dissatisfaction with the rigour of the law in this area.

Common sense approach

The only significant empirical research that has been done (W Young, "Rape Study: A Discussion of Law and Practice" Vol 1 Feb 1983) indicates that the legislation is working effectively to achieve its objectives of preventing intrusion into the complainant's sexual history. Judges and other members of the legal professsion, at least, appear to be of the view that reform of the law has decreased the amount of cross-examination about prior sexual history and has reduced the complainant's distress, without any corresponding cost of greater injustice to the accused or more focus on the character or reputation of the complainant in non-sexual matters. This probably bears testimony to the common sense approach adopted by the Courts.

The study also pointed out, however, that while the unauthorised cross-examination of a complainant was rare, the issue was nevertheless raised in some way during prosecution and defence evidence in just over half the cases surveyed without any application for leave having been granted. And that while this often seemed unavoidable, some evidence which was held to be inadmissible appeared to subvert the purpose of section 23A, such as where the accused's opinion of the sexual reputation and general sexual propensity of the complainant was included in his statements to the police and was therefore read out in Court. (This practice is not in technical breach of the section as "evidence" does not include unsworn statements: *R v Evans* [1962] SASR 303; *R v Robertson and Mihailov* [1978] 17 SASR 479.)

The problems indicated by the study at the preliminary hearing stage have been largely overcome by the Summary Proceedings Amendment Act (No 4) 1985 which places a general prohibition on oral testimony by the complainant and examination or cross-examination on the written statement provided. A District Court Judge, rather than relatively untrained Justices of the Peace, is required to preside over the hearing. This should ensure that the new rules are enforced. The protections for the accused, that oral evidence may be ordered if there is no a sufficient case to answer otherwise or if it is in the interests of justice to do so (s 185C(1)(b)) appear to be adequate. It might be argued that such a change would affect the defence's ability to properly test out the prosecution's case but the level of prejudice seems acceptably small given the embarrassment spared to the complainant.

Despite the restrictive fetters that have been placed generally on the trial Judge's discretion, there is room yet for latitude. In *R v Bills* [1981] 1 NZLR 760, 765 the Court of Appeal, while acknowledging Parliament's intention, still put the emphasis squarely on the trial Judge's discretion,[9] albeit within the framework of the Act. The decision shows that the exercise of the discretion may not be viewed in isolation from the conduct of the parties. There is no obligation on the Judge to take the initiative to change his ruling if the circumstances change, when the defence has been content with that ruling. The prosecution's subsequent reliance, in that case, on medical evidence of recent intercourse as assisting the corroboration of the complainant's evidence meant that had leave been sought then to question whether a specific act of intercourse had occurred that night with another man than the accused, it would probably have been granted.

But the decision to apply for leave was counsel's to make and tactically held "inherent danger" for the accused if granted. If the complainant had denied such intercourse, the jury might well have believed that only the accused could have been responsible for the evidence of recent intercourse and that any verdict of attempted rape would be impossible to reach. The failure of one tactical option could not be remedied by arguing that the s 23A discretion had been improperly exercised. The case turned on identity not consent and the sexual experience of the complainant with a person other than the accused did seem to have the required relevance to that fact in issue because of the contemporaneity in time involved. The non-specific cross-examination sought earlier however did not have such relevance. The defence would not have been prejudiced by the general prohibition if it had applied again to cross-examine on the specific episode as the evidence unfolded.

Foundation for applications

The need to ensure a specific foundation for any application for leave under section 23A was borne out in *R v Uiti* [1983] NZLR 532. McMullin J noted that:

> Because section 23A is intended to prevent general cross-examination of a complainant with a view to eliciting some matter which might be helpful to a defence of consent, it is not every act, circumstance or occasion which will provide a justification for the making of an order. Consequently before a Judge is asked to grant an application under the section, material setting out time, place and circumstance upon which the proposed cross-examination is to be based should be placed before him. In the light of that material he can then determine the relevance and importance of the questions to be put.

It was argued that the trial Judge's decision not to allow cross-examination of the complainant was inconsistent with his later decision

to allow the appellant to give evidence of his observation of the complainant's near-simultaneous sexual experience with a number of members of the Mongrel Mob. But counsel for the defence did not provide any detailed information as a foundation for his proposed cross-examination and probably information of sufficient particularity never came within his grasp to make an application later in the proceedings. The alleged incident with the Mongrel Mob had occurred some nine months previously and Uiti had not even been positive as to the identification of the complainant. Given that at the time the trial Judge made his decision the evidence pointed towards the use of violence to overcome consent, the refusal to allow indeterminate cross-examination was upheld even if the vague allusions of the appellant might otherwise have provided a suitable foundation if a further application had been made pursuant to s 23A(6). (No concluded view was reached on this point.)

Dissatisfaction seems to have been expressed at the trial Judge allowing Uiti to give his evidence at all by the approval of the English Court of Appeal's decision in *R v Viola* [1982] 1 WLR 1138 which was said to be distinguished both by the Court being given the very statements of the witnesses upon which the proposed questions were based and by the fact that the other episodes were so close in time and place to the happening of the alleged rape as to be "of the greatest relevance" to the issue of consent. The relevance of the disputed evidence in *Viola* is fact rather dubious, with respect. In *Viola* leave was granted to cross-examine the complainant about an incident a few hours before the alleged rape when two friends of the complainant's live-in boyfriend had drunk a lot of alcohol with the complainant, in the boyfriend's absence, and supposedly had the "come-in" from her. She allegedly stroked one of them on the back and invited one or the other to try out her new bed.

It had been argued, *inter alia* by defence counsel that there was a similarity between the accused's entry into the complainant's dwelling and that of the two men. As well as not accepting the alleged incidents proximity in time, the Court in fact did not express any view on the matter. It can be said, however, that even if the complainant hardly knew the other man any better than she knew the accused, the circumstances surrounding the entry into the maisonette were rather different. It was not surprising that the complainant should invite in her boyfriend's friends as it was a joint home at the time. A back rub and a flirtatious comment could also hardly be seen as sufficiently similar to alleged intercourse, on any view of relevance. Similarly for another incident which could be adduced that nine hours after the alleged rape there had been a sighting of a male, naked save for slippers, in the complainant's dwelling. The Court in *Viola* does seem to have been influenced by rather spurious considerations that it took nearly three days for the complainant to report the alleged crime and, not relevant at all to the first episode, that injuries to the complainant's face observed when she reported the incident were not noticed by other witnesses shortly after she had been allegedly raped.

On the other hand the allegations in *R v Uiti* (supra) were not "of the greatest relevance" but they were not expressly stated to be insufficiently relevant by the Court of Appeal either. It appears that a fairly expansive view was taken of the relevance needed to satisfy s 23A(3) although any conclusions are necessarily tentative. A common sense approach recognising the importance of the accused's subjective belief, however misinformed, seems to have been taken.

Evidence of virginity

A decision more in keeping with the spirit of the legislation was given by Eichelbaum J in *R v Warren and McGhie* (1983) 1 CRNZ 106 when leave to cross-examine the complainant on her evidence in the depositions that prior to the alleged rape she had been a virgin was refused. In His Honour's view, the evidence should never have been given in the first place and evidence to rebut it was not regarded as falling within s 23A(4). Firstly, on technical grounds it was questionable whether the complainant's evidence was evidence of "any witness". While "complainant" is separately defined in s 23A the interpretation of Eichelbaum J does, with respect, seem to be too restrictive of the scope of the rebuttal evidence provision. Secondly, it was uncertain whether the complainant's lack of sexual experience was "sexual experience" within the meaning of s 23A(4)(a)(i). (Cf Wells J in *Ex Parte Stephenson* [1977] 17 SASR 165)

On this point it might be thought that the distinction between rebutting a denial that the complainant had intercourse with someone other than the accused or that she had a "good" sexual reputation, and rebutting a protestation of virginity is rather fine. However, the more important aspect of the decision was that s 23A(4) was construed only to apply when it was "unfair" to the accused that rebuttal evidence should not be called. Presumably, determination of this will be based on similar policy factors to the rest of the section, it not being sufficient where the rebuttal has only some tenuous relevance to a fact in issue. Fairness to the accused did not necessitate the calling of evidence before a tribunal that had not even heard the original evidence. (See also *R v McClintock* CA 39/86 (unrep))

Section 23A as a whole was construed to apply to stages in the total progress, supported by the wording of s 23A(6)(a) that an application for leave to adduce the restricted evidence may be made:

> . . . before or after the commencement of the proceeding . . ."

If "proceeding" had the arguably wider meaning of the whole trial process then the section would encompass an application under s 23A(2) even before the information was sworn, an obvious impossibility. The construction adopted by Eichelbaum J was further reinforced by the wording of s 23A(6)(b), and the dictionary definition of "proceeding" as ". . . any step taken in a cause . . ." (*Shorter Oxford Dictionary*)

It was not accepted that otherwise the statutory test of

relevance in s 23A(3)(a) was met by the fact that the complainant may have lied as to her lack of sexual experience. There was ample opportunity on the other evidence to examine the complainant's credibility and to merely allow questioning would not resolve the issue one way or the other. Being a collateral issue, the complainant could simply deny the other man's alleged account, and even if the lie were admitted, that had no bearing on the central issue of identity. Notwithstanding the particular differences between the New Zealand and the English legislation, approval as a "useful test" was expressed of the statement of May J in the English case of *R v Lawrence*[10] that for evidence of sexual history, the Judge must take the view that:

> . . . it is more likely than not that the particular question or line of cross-examination, if allowed, might reasonably lead the jury, properly directed in the summing up, to take a different view of the complainant's evidence from that which they might take if the question or series of questions was or were not allowed.

The complainant's credibility may still be undermined, as evidence to this effect will on occasion be sufficiently relevant to facts in issue. The test of the jury "reasonably . . . tak[ing] a different view of the complainant's evidence . . .", albeit buttressed by the Judge being able to point out the dubious inferences, does not appear particularly stringent. Again a common sense approach ensuring a fair trial for the accused seems to have been adopted, reading down blanket prohibitions and elevating the requirement of what is in "the interests of justice" in s 23A(3). The approach is consistent with the rest of criminal law.

Subjective belief

In two recent contemporaneous decisions the Court of Appeal has had occasion to review the application of s 23A. In *R v Daniels and Tihi* (CA 30/86, 31/86 August 1986) the importance of the accused's subjective belief was stressed. (Reasonable grounds for the belief were not then required.) The trial Judge had ruled that evidence of the grounds of Tihi's belief that the complainant was "like that" (in his words in response to a Crown question) from supposedly having been present when she had had intercourse three nights earlier with another of her brother's friends after only the briefest of acquaintances, went only to infer propensity. Cooke P, delivering the Court's judgment, held that the evidence had relevance beyond inferring propensity to the accused's actual belief in consent. However, with this more expansive approach was the recognition that some degree of similarity in the facts should be present. (The reasoning for Cooke P is similar to that of his judgment on this point in *R v Davis* [1980] NZLR 25. See also *R v Katipa* CA 225/85 (unreported) and *R v Avery* T1/87 Eichelbaum J HC New Plymouth 11/5/87 (unreported).)

The Court did not indicate the extent of this apart from holding that the previous episode was "in quite different circumstances" to the intrusion into the complainant's house of Daniels and Tihi, with the question being what Tihi believed after the complainant had intercourse with Daniels. It was not stated that any similar fact rule "in reverse" should apply before adducing evidence of the complainant's conduct but nor was it allowed that the accused should be able to infer his view as to the woman's readiness to consent from very dissimilar conduct. The result is in accord with criminal law generally and indicates, it is submitted, that s 23A has not been interpreted as imposing an exceptional rule.

It was also held, *obiter*, by Cooke P that the section could not be allowed to inhibit clarification of relevant evidence which arose naturally in the course of the trial. That is, if counsel had applied for leave for Tihi to state his grounds for belief after Tihi's comment upon cross-examination by the Crown. However, an opportunity for rebuttal, would, in fairness, be afforded to the complainant, even though it was not the truth of the grounds for belief but the belief itself which was in issue. This approach has the potential to further limit the application of s 23A, albeit with the rider that the ascertainment of the accused's subjective belief should be grounded in fact. This is now dictated (perhaps more stringently) by statute with the requirement of reasonable grounds for belief (Section 128(2) and (3) of the Crimes Act 1961, as amended in 1985) in consent.

Sufficient proximity in time

In *R v McClintock* CA 39/86 (unrep) an incident has supposedly occurred three or four weeks before the alleged rape, when at a party in the same flat the pregnant complainant and one of the accused's brothers has consensual intercourse known to both accused. It was held by the Court of Appeal (approving the application of the test in *R v Viola* [1982] 1 WLR 1138 for New Zealand law) that acts of intercourse with other men may be so closely connected with the alleged rape, that evidence of those other acts may be probative of the fact that the complainant consented to intercourse with the accused, or of the fact that the accused believed the complainant to be consenting. The contrast with evidence of similar fact being used against the accused was not, however, examined. The decision, at least, is not inconsistent with the imposition of a lower threshold of relevance. The alleged earlier episode was regarded as being of only marginal relevance and lacking sufficient proximity in time, and, more importantly, lacking sufficient similarity in circumstances. The evidence of the complainant appears to have been accepted without question with "consensual intercourse with one man, in the latter stages of what seems to have been a light-hearted party . . ." contrasted with "the violent and brutal intrusion of which the girl spoke on the occasion of the crimes".

It was acknowledged that the evidence of the earlier incident might have had some minor relevance to counter any suggestion that a pregnant woman would not willingly engage in intercourse, something which went beyond mere propensity. However, in light of the Judge's summing-up, that evidence was only of tenuous relevance. The argument that the evidence countered the inference that the complainant would have been unlikely to be willing to have intercourse with a man met for the

first time went hardly, if at all, beyond propensity reasoning.

Evidence attacking the complainant's credibility was accepted as being sometimes, as a question of degree, directly relevant to facts in issue and thus satisfying s 23A(3)(a), (approving the *dictum* of Lord Lane CJ in *R v Viola* (supra). Once again, s 23A was seen as not inhibiting questions or evidence relating to credit. However, on the facts, the vague evidence from the complainant, even if it had included a denial in the lower Court of intercourse in the month before the night in question with someone other than the co-accused, was, as in *Warren and McGhie* [1983] 1 CRNZ 106, not sufficient to have a significant bearing on the essential credibility of the complainant's testimony relating to the crucial episode.

In sum the New Zealand cases all show a rather flexible interpretation of s 23A, seizing the warrant of the "interests of justice" test in s 23A(3) to frame matters in terms of basic relevance, bearing in mind the need to ensure a fair trial for the accused. Evidence of sexual history is not exceptional but in accordance with normal principles of placing the alleged victim's conduct or character in issue. Evidence relating to credit "alone" is sometimes not excluded because it is not possible to view it in isolation from facts in issue. The statutory provision thus appears unnecessary and, on the surface, overly restrictive. It might have achieved its purpose of mending old bad habits but it is submitted that a legislative direction imparting more discretionary powers would achieve the same result, as reflecting the Courts' justifiably flexible approach.

Conclusion

It appears that the level of regulation imposed by Parliament when it enacted s 23A has not worked injustice for the accused. But this is in part a tribute to the Courts' consistent approach in not viewing sexual violation as an exception to fundamental principles of criminal law and evidence.

The reality is that prior sexual conduct may sometimes be relevant, that there are sometimes those "kind" of girls and that people often act in similar ways. The danger is to overstate this, and the typically prejudiced jury needs to be carefully directed. It is an illusion that each sexual act always has a unique meaning but it is equally wrong to simply smear the character of the witness by recounting prior dissimilar sexual episodes. For this is merely an appeal to prejudice and is unlikely to indicate consent, particularly in the light of changing sexual mores and attitudes in the community. Perhaps in the future revised attitudes will be so prevalent that defence counsel will not even seek to "try it on", and the purpose of restricting sexual history evidence will be confined to protecting the sexual privacy of the complainant.

Changing attitudes in society are also making the accused's belief in consent based on the reputation of the alleged victim less relevant, but the accused's subjective intention must be of paramount concern as it is in criminal law generally. The requirement of reasonable grounds for belief in consent in New Zealand is argued to be a retrograde step, to be only logically viewed in the light of public hysteria about sexual crimes. If it's time to change our conceptions of justice more away from the accused, then the shift should be across the board and not in an ad hoc manner in response to public outcry. Even with reasonable grounds for belief, however, it is submitted that the person on the QEII hydroslide (a suggested updated version of the classic "man on the Clapham omnibus" test) would still find the reputation or sexual history of the complainant to be relevant to whether she consented or not. The ideal feminist view is somewhat in advance of normal attitudes or reality. Accordingly, it has no place in criminal law. The feminist emphasis should be on education, changing public perceptions and helping those women who are generally used by men.

Manifestly irrelevant evidence should not be admitted however, but it is submitted that the Courts do not need their hands tied in achieving this. If a direction is felt to be necessary, a discretionary one along the lines of that existing in England for *all* evidence of sexual history (including that involving the accused) is all that is necessary. The considerable resources that have been wasted on producing elaborate rules to date have not altered the position that sexual history evidence is not an exception to traditional principles of criminal evidence. □

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1 *R v Cockcroft* [1870] 11 Cox CC 410; *R v Riley* [1887] 18 QBD 481. Including evidence of episodes of intercourse after the alleged rape: *R v Aloisio* (1969) 90 WN (Pt 1) (NSW) 111 [CA].

2 Obiter, per Stephenson LJ in *R v Krausz* [1973] 57 Cr App R 466, 474; *R v Greatbanks* [1959] Crim LR 450, Cf *R v Thompson* [1951] SASR 135.

3 See generally the article by R Pattenden [1986] Crim LR 367 and the cases cited by her.

4 *R v Viola* [1982] 1 WLR 1138; Approved by the New Zealand Court of Appeal in *R v McClintock* CA 39/86 (unreported).

5 See, for example, Z Adler [1982] 45 MLR 664 — the figure was 46.3% acquitted in her sample.

6 Assumed to be the case by Wells J in *R v Gun; Ex Parte Stephenson* [1977] 17 SASR 165, 182. See also *R v Byczko (No 1)* (1977) 16 SASR 506 Cf *R v Warren and McGhie* (1983), 1 CRNZ 106.

7 [1977] 17 SASR 165, 184, on the former section 34(i) of the Evidence Act 1929 (SA). The test has been replaced in South Australia.

8 This appears to have been contemplated by Eichelbaum J in *R v Warren and McGhie* (supra) and by the Court of Appeal in *R v McClintock* CA 39/86 (unreported).

9 In approving the comments made by Roskill LJ in the Court of Criminal Appeal in *R v Mills* [1978] 68 Cr App R 327.

10 [1977] Crim LR 492, 493. Approved by the English Court of Appeal in *R v Mills* [1979] 68 Cr App R 327, 330.

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merged companies.

The Amendment is being used in circumstances which fly in the face of accounting convention. There have been criticisms by accountants that the Amendment is being artfully used to improperly boost profits.

The legal criticism is that the Amendment is in direct conflict with the creditors' protection provisions in s 64.

The Amendment permits a premium arising from a takeover to be recorded as a revenue item when it is better viewed as capital. As a revenue item it is distributable to shareholders by way of dividend, effectively reducing the capital resources available to meet creditors' claims. □