THE NEW ZEALAND
LAW
JOURNAL
PUBLISHED BY BUTTERWORTHS DECEMBER 1996

COURTS OR COMMITTEES?

One of the first things an evil, dictatorial government would do would be to eliminate the differences between Courts and other decision making bodies. Now it seems that the Judges are bent on this goal.

In the High Court Justice Gallen decided that the Human Rights Committee under the International Covenant on Civil and Political Rights was a "judicial authority" for the purposes of the Legal Services Act so that a person taking a complaint to the Committee was eligible for legal aid.

Judicial authority has always been believed to be composed of a number of elements, none of which is shared by the Human Rights Committee.

First, judicial authority must be exercised by judicial officers. The members of the Committee are not, in that capacity, Judges. They do not have security of tenure, being elected by the States Parties and being eligible for re-election. Some are government servants. Neither their remuneration nor the Committee's budget is protected by law, in fact both are the subject of constant political wrangling.

Secondly, judicial authorities do not, in that capacity, carry out non-judicial tasks. Although High Court Judges may be appointed to Royal Commissions for example, it is not the High Court carrying out the inquiry. Conversely, the Committee does carry out non-judicial functions. In particular it issues "General Comments" on various issues which look suspiciously like pre-judgments of matters which have not yet reached it formally.

Next, a judicial authority issues binding and final decisions which are automatically effective. The Human Rights Committee does not. Its rulings are binding on the government in international law only. If they require a change in the law of New Zealand the government cannot commit Parliament in advance to passing that law. There is simply no comparison between that situation and the analogy the judgment draws with the Privy Council. In form that body only advises the Queen but constitutional convention requires the Queen to follow its recommendations. The same conventions prevent the government from committing Parliament to a particular course of action.

Nor is there any enforcement mechanism. In fact the government can repudiate the Covenant altogether.

His Honour seemed to think that because the government had decided to grant the right of individual complaint, Parliament must have intended to include the Committee in the Act. This is just to brush aside the distinction between government and Parliament. In the end the argument which won the day was that legal aid ought to be available as the right to complain to the Committee would otherwise be a hollow right. (I look forward to hearing someone argue that the right to private education is a hollow right on the same ground.) This is clearly judicial legislation, just another example of what we see time and again in the context of ACC and social welfare. Parliament allocates a budget for an activity and rules are drawn up so as, amongst other things, to fit the amount of money available. When a hard case comes up, someone who falls just outside the line, the Judges show themselves ready and willing to dish out a bit more of the taxpayers' money to the supplicant.

Also interesting was the reaction of the Legal Services Board. The Board will probably not appeal, it said. This again reflects what occurs in other areas of governmental activity. The commitment of public bodies to fighting cases is frequently suspect and appeals will not be mounted if that requires taking a hard-hearted or politically incorrect line. After all why should they worry? It is not their money that is being dished out. Just everyone else's.

Meanwhile, up the road, the Court of Appeal was turning itself into a committee. In a case between two private parties, which was required by Act of Parliament to be conducted in private, lobby groups were admitted and allowed to make submissions. The Crown was asked to provide advice on a matter of statutory interpretation. The Judges seemed inclined to open matters which the parties had agreed not to contest and on which no evidence had been called.

If the Crown is to be allowed to advise the Court how to interpret this statute, why not every statute? If some lobby groups are to be allowed to make submissions why not everyone who wishes to make a submission? If we are to consider issues not raised by the parties, why not turn the job of interpreting the law over to select committees?

There are a few differences between Courts and select committees. One is that anyone criticising the track record or belief system of a Judge, as opposed to the words of a judgment, is at risk of being found in contempt. The other is that Judges are paid three or four times as much as MPs. This could indicate that they are expected to do a different job. It does not take long to work out the answers to the questions above and they are all reasons why Courts should not indulge in these kinds of activities. We do not pay Judges huge salaries to be followers of fashion.

PS. There is a positive aspect to the Human Rights Committee decision. The judgment exposes to the light of day the great effective power of the Committee. It can consider a complaint against New Zealand legislation and recommend that it be changed. The Privy Council cannot do this. For some reason this was never mentioned by the government during the Privy Council debate. It exposes the "national sovereignty" argument in that debate for the nonsense it always was. ❑

THE BILL OF RIGHTS AFTER *BAIGENT*

Bruce Pardy, Victoria University of Wellington

gives Mark Anthony's response to the Baigent *case. This was first aired at a debate held by the New Zealand Institute of Public Law.*

Friends, lawyers, countrymen, lend me your briefs;
I would like to bury *Baigent*, not to praise it.
The harm that hard cases do live after them,
The good is felt by the victor alone;
So it is with *Baigent*.

Come I to speak of the decline of an institution
Which, before *Baigent*, stood at the top
Without equal, unchallenged in its power
to make the law.
I speak of Parliament, supreme.
But then Parliament made an ambitious slip.
It passed a law called the Bill of Rights,
A law that was an ordinary statute.

Then the plaintiff
Pleaded the police had got it wrong,
That they entered sans licence, sans cause
sans excuse,
Just to have a look around.
If it were so, it was a grievous error,
And grievously should they be made to answer for it.

And so we have in *Baigent* a just result,
Which I come not to criticize.
The same result on different grounds would
give me cause
To sing the praises of this case, for its wise result,
its clever law,
Its sense of right and wrong.
We could have had a normal case, fit shapes to shapes
For breach of statutory duty
Since the Bill of Rights is an ordinary statute.

Twas not, of course, to tort or normal remedy
That life was given, but to new law that received
this touch;
The Court determined that our fine citizens
Need not resort to tribunals in foreign lands
But can be served by Kiwi Courts
For remedy to global human rights.
Had I the skill I would show you such,
In black and white, in the Bill of Rights,
But I know not where to find such a guarantee
It must be there as plain can be, for that's how
statutes work,
They change the common law only as they say they do,
And in *Baigent*, the Bill of Rights is an ordinary statute.

Of course, the remedy is not there in the words,
It must come from elsewhere - where to look?
The Court relied upon the laws of other places,
India, Ireland, Trinidad and Tobago
Fundamental rights and public remedies
Constitutional provisions all,
All, except in New Zealand,
Since, in *Baigent*, the Bill of Rights is an ordinary statute.

The decision speaks of many cases from these lands:
Bivens, *Byrne*, *Maharaj*, and *Nilabati*
Fine cases, highly praised and relied upon,
Cases interpreting constitutions all,
All, except for *Baigent*,
For in *Baigent*, the Bill of Rights is an ordinary statute.

The creation by our finest Court of a remedy
Called breach of Bill of Rights
Cannot denote a place supreme
For any particular enactment,
Because in *Baigent*, the Bill of Rights is an
ordinary statute.

I am too harsh. To achieve this just result
Other Acts of Parliament had to be
Overcome or stepped around,
Those that provide immunity for the Crown
Which would apply if the remedy was for
statutory breach,
This could not be, or else the police would win the day,
So how to get around the other things that
Parliament has said?
It must be to place one beyond the other,
Not to make the Bill supreme,
Merely beyond the reach of other things,
Contrary to its own description.
But in *Baigent*, the Bill of Rights is an ordinary statute.

I come not to disprove what my friends will speak,
But I am here to speak what I do know.
You all have loved the rule of law, not without cause;
What cause prevents you now to grieve its loss?
For means and ends are different things;
And so I close my case and leave the floor,
Not that I love *Baigent* less,
But that I love Parliament more. ❑

FIDUCIARY'S BREACHES AND EMPLOYEE INDEMNITIES: TWO ASPECTS OF LAW FIRMS' LIABILITY

Duncan Webb, Lecturer, Bell Gully Buddle Weir Fellow, Victoria University of Wellington

discusses the liability of staff solicitors and the extent of the defence of no causation

Whether a solicitor in breach of their fiduciary duty to a client can, in defence, plead lack of causation, and whether an employee solicitor in a law firm is liable to the firm for any loss that the firms suffers by virtue of the solicitor's negligence, are questions that most would prefer to deal with on an academic basis only. These were the issues before the Court in *Everist v McEvedy* (unreported High Court, Christchurch, 12 June 1996 AP 62/95, Tipping J on appeal from Noble DCJ).

THE FACTS

The questions arose due to the conduct of an employee solicitor, Mr McPhail, who was acting for his sister-in-law in certain bridging finance and sale transactions of real estate, and also for an earlier mortgagee, Mrs McEvedy. The mortgagee discharged the mortgage over the property without repayment, and without taking substitute security. This was done in ignorance of the fact that later mortgagors were paid out, and that there was insufficient equity to pay all secured parties. It was the failure of the solicitor, McPhail, to advise of this shortfall that was found to be a breach of fiduciary duty for which the firm was liable. The judgment covers two actions arising from these facts. The first by the client, McEvedy, against the principal Everist for breach of fiduciary duty. The second by Everist against his employee solicitor, McPhail claiming an indemnity for any amounts the Court awarded as payable to McEvedy.

CAUSATION AND BREACH OF FIDUCIARY DUTY

The first matter considered by Tipping J is of considerable significance; whether a fiduciary can plead a lack of causation in defence to a claim based on the breach of that duty. In most areas of the law it is fundamental that one will only be liable to compensate for loss which is caused by the wrongful acts complained of. Claims for breach of fiduciary duty have traditionally been seen as an exception to that rule and lack of causation has been stated to be no defence: *Brickenden v London Loan and Savings Co* [1934] 3 DLR 465. Such an exception has been justified on the basis that the duties of trustees and fiduciaries are strict and such absolute liability will be a deterrent to such breaches. Furthermore the weaker party in such a relationship ought not to be put to proof when they may not be in possession of the full details of the cause of the loss.

TWO LIMITS ON THE DEFENCE OF NO CAUSATION

Tipping J relied drew on dicta from *Target Holdings v Redferns* [1995] 3 All ER 785 in finding that whilst such reasoning may be appropriate in a trust situation where strict duties attach to the position of trustee, and the trustee in usually in exclusive possession of the information in respect of trust assets, it may not be entirely proper to transfer that reasoning to all fiduciary relationships.

The idea that a person can be liable for loss that they did not cause (even if they did act wrongly) has caused difficulties. The result has been a slow erosion of the strict application of the *Brickenden* rule. The weakening of the rule can be seen in a number of cases including *Witten-Hannah v Davis* [1995] 2 NZLR 145 and *Haira v Burbury Mortgage Finance and Savings (in rec)* [1995] 3 NZLR 396, as well as *Target*. It seems now to be the case that causation is a necessary ingredient in an action for breach of a fiduciary relationship, however the tests for causation are significantly different from those in other areas of the law in two respects.

First, the onus will be on the fiduciary to prove that the breach complained of did not cause the loss. It is therefore presumed that the breach caused the loss until evidence can be adduced to demonstrate otherwise. Thus Tipping J stated that "the errant fiduciary cannot invite speculation. There must be a proper evidentiary foundation for the conclusion [of lack of causation] that the Court is asked to draw", and later "Under the law as earlier described the onus is on the solicitors to show that events would have turned out exactly as they did even if Mrs McEvedy had received competent independent advice or full information".

Second, it appears that whilst a fiduciary will have a defence if they can show a lack of causation, this must be more than showing simply that the loss was not foreseeable, or that the damage was remote. It was observed by Lord Browne-Wilkinson in *Target*, and emphasised in *Everist*, that it only needs to be shown that there was some causal nexus between the breach and the loss and that the loss would not have occurred "but for" the breach. Put another way, it must be shown that the loss would have occurred even if the duty was not breached. In *Haira* this was formulated as having to show that the breach of the obligation was material to the transaction.

The question is not, therefore, whether the loss was a foreseeable and proximate result of the breach. Rather it is the lower test of whether the loss would have been sustained if the breach had not occurred.

STRICT RULE DISPLACED

The rule that no inquiry can be made into whether a breach of a fiduciary relationship was causative of the loss for which compensation is sought has been displaced. As Tipping J stated in *Everist* "the pure *Brickenden* approach has the door entirely shut. *Haira* appears to have opened the door, not to admit speculation, but to admit a conclusion based on reasonable inference". Whilst causation is presumed to exist, it is not conclusively presumed. If evidence is presented which shows the loss would have been sustained in any event, it is open to the Court to decline to grant relief.

THE RIGHT TO CLAIM FROM AN EMPLOYEE

Unlike many errant young practitioners, Tipping J considered in some depth the question of who was ultimately liable for the breaches of a staff solicitor.

It was accepted that the client, McEvedy, was entitled to claim against the firm for the breach of fiduciary duty of the employee solicitor by virtue of the doctrine of vicarious liability. However the principal claimed recovery from the employee for the amount payable to Mrs McEvedy. This claim was based on the well established principles in *Lister v Romford Ice & Cold Storage Co* [1957] AC 555.

Lister established that a duty is implied into every employment contract that the employee will exercise care and skill in the execution of the tasks incident to the employment, and that the employer is entitled to seek an indemnity from the employee in respect of any loss occasioned by a breach of that duty. It was noted that these principles were applied in New Zealand in *Bromwich v Pacific Commercial Bank Ltd* [1988] 1 NZLR 641 where the negligence of a Post Office worker led to the loss of a parcel containing cash. Although a statutory defence applied it was held that had that not been the case *Lister* would have applied and enabled the Post Office to claim from its negligent employee.

AN IMPLIED INDEMNITY FROM THE EMPLOYER?

The employee solicitor was, therefore, prima facie liable to his employee for the loss sustained. It was, however, argued that a term could be implied into that particular employment contract to the effect that the firm indemnified the employee from any claims that might be made against him in respect of conduct in the course of his employment (except in the case of fraud or dishonesty), thereby displacing the *Lister* rule.

In the District Court Judge Noble found that such a term could be implied from the particular facts of this case under the principles in *BP Refinery Westernport Pty Ltd v Shire of Hastings* (1977) 19 ALR 363. Namely that the term was reasonable, necessary, obvious, clear and consistent with the rest of the contract. Such a finding is clearly inconsistent with *Lister* which decided that as a matter of law there was a term implied in every employment contract to the opposite effect: that the employer had a right of indemnity from the employee.

Tipping J rejected this finding of the District Court Judge. He did so on the basis that the term was not necessary to the contract, and also doubted whether it was sufficiently obvious. In so finding His Honour stated that "The contract, without the term, would still work, albeit on a less advantageous basis to the employee".

His Honour did, however, find that a term could be implied into the contract by virtue of a usage of trade or custom. In making this finding he applied the test laid down in *Woods v LJ Ellingham & Co Ltd* [1977] 1 NZLR 218. That test has five elements that bear a striking resemblance to those of the *BP Refinery* test for terms implied by fact. They are that the term must be notorious, certain, reasonable, clear and proven, and consistent with the express terms. Tipping J noted that the doctrine of terms implied by custom might be viewed as a specialised kind of terms implied by fact. This is accurate in so far as in both situations the Court is seeking to give effect to the presumed intent of the parties, or at least what the parties would have intended had they turned their minds to the matter.

the President of the New Zealand Law Society, Austin Forbes QC, gave evidence to the effect that law firms accept responsibility for the misfeasance of their employees

It is of note that for a term to be implied by custom the onus is on the party asserting the custom to prove it, and evidence will have to be called to substantiate such a claim. In the present case the President of the New Zealand Law Society, Austin Forbes QC, gave evidence to the effect that law firms accept responsibility for the misfeasance of their employees. That evidence was not challenged.

WHICH IMPLIED TERM PREVAILS?

Another point of interest is that the term implied by custom was in direct conflict with the *Lister* term which is implied by the common law. Tipping J did not, however, see this as a bar to finding the term to be implied by custom. This meant that the term implied by custom effectively displaced the term implied by common law. This appears sensible in that the more specific term prevails over the general one.

This issue was further complicated by Tipping J opining that whilst a term implied by custom will displace the *Lister* rule, a term implied by the particular facts of the case would not. The basis for this distinction is difficult to see. Clearly the parties could, by express agreement, displace *Lister*. Furthermore the Court found that if the parties' intentions could be inferred from custom in the trade then this intention could equally displace the common law rule. Why then could the intention of the parties inferred from the circumstances surrounding the case not be equally capable of ousting the term implied by the common law?

A NEW TERM IMPLIED BY CASE LAW

It was also noted that the Court has now taken judicial notice of the existence of this custom in the legal profession. If such a matter were to come before the Courts again it would be up to the party asserting the custom to be other than that found in this case to bring evidence to prove it. The term that every firm indemnify its solicitor-employees for loss which may be sustained by the negligent discharge of the duties is, therefore, now confirmed. ❑

DIRECTORS' PERSONAL LIABILITY

Brian J D Gould

assesses the likely impact of s 135 Companies Act 1993

Concerns have been raised that s 135 of the Companies Act 1993 has the potential to expose directors to excessive risk of liability, or to cause them to act too cautiously, for example see R D Deane "Besieged by Duties" *The Company Law Conference*, 1994 New Zealand Law Society at 3. Also see Hodder (1994) 762 TCL 17, "Fortex Failure and Directors' Duties" (1994) at 1:

> the effect of s 135 is "that the well advised director will be extremely risk-averse; most new ventures, and many of those already established involve both the risk of failure and the use of loan capital. All of which undermines the realities of capitalism affirmed in the 1993 Act's long title".

Section 135 is substantially wider in scope than its predecessor s 320(1)(b) Companies Act 1955. Section 169(3) states that the duties in s 135 are duties owed to the company but not to shareholders. It is clear from these provisions, and the provisions of Part XVI (liquidators) that this is not a duty directly owed to creditors. However, the creditor receives the benefit of those duties in the event that the company is liquidated, and creditors are entitled to bring Court proceedings to liquidate companies. Creditors can apply to the Court for an order that the company be put into liquidation if the company is unable to pay its debts, or if the directors seriously or persistently fail to comply with the Companies Act or if it is just and equitable that the company be put into liquidation (ss 241(2)(c), 241(4) and 288). Once the company is in liquidation, the Court may, on the application of the liquidator, or any creditor, order the directors who contravened their s 135 duties to make payment into the liquidation assets of the company or to pay the creditors directly (s 301(1)(h)(ii) and (c). These factors, and others (see *Anderson's Company and Securities Law* v 1 para 135.04), support the contention that s 135 is wider in scope than its predecessor.

The core concept "recklessness" in s 320 of the 1955 Act has been replaced by the perhaps more measured words "likely to create a substantial risk of serious loss" (under s 5(f) Acts Interpretation Act 1924 the heading "reckless trading" does not affect the interpretation of s 135).

Paraphrasing, s 135 stipulates that:

> A director of a company must not agree to the business of the company being, or cause or allow the business of the company to be, carried on in a manner likely to create a substantial risk of serious loss to the company's creditors.

The long title of the Companies Act 1993 asserts that the Act is intended to achieve a trade-off by:

> allowing directors a wide discretion in matters of business judgment while at the same time providing protection for shareholders and creditors against the abuse of management power.

This balancing of the director's business discretion against the protection of creditors and shareholders from abuse of that discretion appears to be intended to help achieve the long title objective of promoting:

> ... the value of the company as a means of achieving economic and social benefits through the aggregation of capital for productive purposes, the spreading of economic risk, and the taking of business risk ....

The reader might expect to see those words reflected in the substantive provisions of the Act. It seems that, by employing the criterion "a substantial risk of serious loss" in s 135, the Act attempted to achieve the trade off by specifying levels of risk and loss which are deemed unacceptable.

However, Deane argues that this criterion seems principled and rational only until one recognises that it turns on just one of the two essential elements of a business decision. As contemporary law and economics literature recognises (see, eg Cooter & Ulen *Law & Economics*, Harper Collins 1988.), business decisions require consideration of both the risk of loss and the prospect of profit, that is both the "downside" and the "upside". Adding the upside to the downside gives risk to a net expectation of gain (or loss). This can be expressed in very simple economic terms.

DOWNSIDE		UPSIDE		NET EXPECTATION
Probability of loss X dollar amount of loss of proposed course of action	+	Probability of gain % dollar amount of gain of proposed course of action	=	The expected monetary value of proposed course of action

With its recognition of the ever present risk of loss in a world where uncertainty is the rule, this analysis leads to the conclusion that the law should ask whether the behaviour of directors is appropriately risky, rather than merely asking whether the behaviour is risky. Can s 135 properly be interpreted to allow appropriate recognition of business risk? This article is concerned with considering this question in the light of the net expectation concept.

Justice Tompkins has discussed Deane's concern, subject to the customary judicial disclaimer regarding opinions of law expressed outside the courtroom. (Tompkins J, "Directing the Directors, the Duties of Directors Under the Companies Act" (1994) 2 Waikato L R 13 at 14 and 27.) He opined that the concern is not well founded as:

> If a risk of loss is reasonably balanced by a prospect of gain, the risk could not be characterised as substantial. In assessing the degree of risk the Courts are likely to

> take an attitude which is commercially realistic. ... This is one of the contexts where there will be reference to the statutory objectives set out in the long title ... the taking of business risks by allowing directors a wide discretion in matters of business judgment.

In effect, Tompkins J would follow the economic approach by requiring the "upside" criterion to be read into the section by interpreting "substantial risk of serious loss" as shorthand for the above economic analysis. That is s 135 would require the director, looking at the probability and magnitude of both gain and loss, to ask whether the net expectation is of serious loss. One commentary however, appears to suggest that the word "likely" is being used not only to capture situations where risk of serious loss already exists, but also those where that risk does not yet exist, but somehow lies latent and "likely" to come into existence. (Hugh Rennie QC and Peter Watts *Directors' Duties and Shareholder's Rights* 1996 New Zealand Law Society, 35.) There is an obvious analogy with the frequent use of a similar formulation in the Commerce Act 1986 (eg s 27 "has or is likely to have the effect") and in the Fair Trading Act 1986 (eg s 9 "conduct that is misleading ... or is likely to mislead"). However, the analogy does not hold. In those two Acts "likely" is used disjunctively, whereas in s 135 "likely" is used conjunctively. The use of the probability term "likely" is puzzling in conjunction with the criterion "substantial risk of serious loss" as that criterion already contains its own probability term ("substantial risk"). Probability terms (such as likely, liable to and risk of) are meaningless unless they refer to an event (eg "serious loss"). In s 135 the probability term "likely" does not refer to any event other than serious loss. Taken literally then, the section is concerned with whether the manner in which the business is carried on will create a "likely substantial risk" of serious loss. Or in other words "a risk of a substantial risk" of serious loss. The presence of "likely" appears redundant.

It is necessary therefore to either dismiss the use of "likely" as redundant drafting or to find a sensible meaning for it. The Courts are slow to treat apparently deliberate words as superfluous (Burrows *Statute Law in New Zealand*, 1992 p 131). In the light of the foregoing, a modification of the interpretation that Tompkins J suggests would attribute to the use of the word "likely" a sensible and appropriate meaning. In the economic terms, "likely" is intended to limit the scrutiny of s 135 to the net expectation created by the conduct of the business. A risk of loss in contravention of the section is not likely unless the net expectation is a risk of loss. It is suggested therefore that "likely" fills the role that Tompkins J would have attributed to "substantial", freeing that word for its role of specifying the probability of the net expected risk, while "serious" specifies the size of the net expected loss.

On this approach, the plaintiff must show that the manner in which the business was carried on was such that the risk of loss was not, in Tompkins J's words, "reasonably balanced by a prospect of gain", or more precisely, the net expectation was loss rather than gain.

Moreover, it seems that the plaintiff cannot prove contravention of s 135 merely by showing that a particular action or inaction did not itself contain sufficient prospect of gain to balance the associated risk of loss. Rather, the plaintiff must take issue with the business as a whole. On its face s 135 is concerned with "the manner" in which "the business" of the company is "carried on". This is in marked contrast with s 136 which, on its terms, is concerned with particular transactions. Section 136 stipulates that directors "must not agree to the company incurring *an obligation* unless the director believes at the time on reasonable grounds that the company will be able to perform the obligation ... ". Accordingly s 135 appears to be concerned with the general policies and practices of the company, rather than particular transactions. (This issue and others are anticipated in Dabnet "Insolvent Trading: Recent Developments in Australia, New Zealand and South Africa" (1995) JBL 282 at 305.) It would follow that the s 135 plaintiff must show that the business as a whole was carried on in a manner in which the overall prospect of gain was not sufficient to balance the aggregate prospect of loss. (While there will be cases where a particular transaction is so large relative to the total business of the company, that it is sufficient to focus on that particular transaction to establish contravention of s 135, the plaintiff will still need to put that transaction within the context of the "the manner" in which "the business" of the company is "carried on". Here there is scope for overlap with the "paper transactions" provision s 129 of the Act.) On any view that must impose a significant evidential burden upon the plaintiff, particularly if the directors have been able to keep records which establish that, on a sensible interpretation of the information reasonably available to them at the time (see s 138), the chances and magnitude of loss were balanced by prospects of gain.

Finally, it is clear from s 162 that, while the company may not indemnify directors for breach of their duties to the company, the Act is no obstacle to the company insuring its directors against liability to the company including liability under s 135 (Sections 135 and 136 do not give rise to criminal liability under the Act: see Part XXI), at least where the contravention of s 135 is merely negligent rather than intentional, (*MacGillivray and Parkington on Insurance Law* 8th ed, Sweet & Maxwell 1988, paras 433, 435, 456 and 475). In that case insurance for s 135 liability will be enforceable under the general law of insurance contracts.

Applying the interpretation contended here, s 135 would not expose appropriately risky directors to excessive litigation risk, or cause them to act too cautiously. Unless one is willing to treat the word "likely" in s 135 as superfluous, and ignore the long title and commercial reality, the current wording cannot sensibly be construed as inviting the plaintiff and the Court to focus on the probability and magnitude of loss to the neglect of the probability and magnitude of gain. However, as Tompkins J said:

> if it is legitimate to balance the risk with the return, it would have been preferably for the section to say so. As it is, the boundaries of the duties under the section will have to be determined by the Court. That is contrary to the purpose of the reform. (at p 27).

That view, the views of other commentators, and the foregoing discussion all demonstrate the lack of clarity of the section. Given the economic importance of directors taking appropriate business risks, it would be helpful to have s 135 amended to clarify the matter. In the meantime, the well advised and appropriately risky director will have to be content with insurance coverage for s 135 liability and keep (yet more) records to establish that the business of the company is and was conducted in a manner in which the net expectation, at the relevant decision times, was gain. While there is a risk that other interpretations will be adopted by the Courts, the most sustainable interpretation of s 135 limits its scrutiny to the net expectation of loss (or gain). ❑

A CONTRACT WITH ITS OWN MEANING ?

Professor D W McLauchlan, Victoria University of Wellington

discusses the judgment of Hammond J in BP Oil New Zealand Ltd v BA Motors (NZ) Ltd

The recent case of *BP Oil New Zealand Ltd v BA Motors (NZ) Ltd* [1996] 1 NZLR 425 raised a difficult yet intriguing issue of contract interpretation. A petroleum products supply (solus) agreement which specified a five year term also stipulated that the buyer must give 12 months' notice of its intention to terminate the agreement "on or after the due expiry date", the apparent intention behind the latter provision being that the contract was to remain on foot until the period of notice had lapsed. Were these provisions inconsistent? What was the duration of the contract? Was it for five years, six years, or for some longer and indefinite period depending on when the buyer gave the requisite notice? In particular, was the buyer still obliged, after the arrangement had continued for nearly six years, to give 12 months' notice?

Hammond J's decision that the maximum period of the contract was six years was noted briefly in this *Journal*: Alan Ringwood, "Terminating a Contract" [1996] NZLJ 204. To the extent that the author commented on the case his view appears to be favourable. However, in the present writer's view, both the approach of the Judge and his actual resolution of the case are open to question.

THE JUDGE'S APPROACH

In the course of contesting the argument of counsel for the plaintiff (BP) that 12 months' notice was still required, counsel for the defendant (BA) sought to rely on extrinsic evidence of certain conduct and communications between the parties both prior to and after the agreement was concluded. It is possible that much of this evidence was unhelpful because it did not provide a reliable indication of the meaning attached by the parties to the particular words in dispute at the time of the contract. However, Hammond J chose to disregard the evidence on the ground that (p 429):

> this is not a case in which this Court should go outside the terms of the agreement itself. Here there were two commercial parties who chose to reduce their negotiations to writing. At least in a case like the present, "the contract" has its own meaning which may not, in the end, comport precisely with what meaning one or other parties (whether a priori, or subsequently) attached to "the contract".

This statement reflects a common judicial assumption that the terms of a contract may have a meaning independent of the intention of the parties – that words may speak for themselves or be self-defining and that any necessary aids to determining the sense of the words are to be found within the four corners of the document. The fallacy of this assumption has been exposed by numerous writers including Professor Corbin who observes (*Corbin on Contracts* 1st rev ed, vol 3, 1971 Supp, para 543A):

> Words, in themselves alone, have no "meaning"; it is always some person who has a "meaning", a person who uses them to convey his thoughts (his "meaning"), or a person who hears or reads the words and thereby receives a "meaning" and understanding (a "meaning" and thoughts that are his own). This latter person may be one who is a party to the agreement, the Judge, or any other third person.

For Corbin it was axiomatic that "[n]o contract should ever be interpreted and enforced with a meaning that neither party gave to it"(para 572B).

On this approach the basic task of a Court when interpreting a contract is to determine the *parties'* meaning or, if that is not apparent, the meaning which reasonable persons in their position would have intended. Either way the terms of a contract can never be interpreted without regard to the surrounding circumstances. These circumstances may show, for example, that at the time of the contract the parties were in actual agreement as to the meaning of the words in question. In such a situation the parties' shared understanding *is* the meaning, a view endorsed (at least where the words, in their context, are "fairly capable of bearing more than one meaning") by the recent decision of the Court of Appeal in *Air New Zealand Ltd v The Nippon Credit Bank* (12 August 1996, CA 48/96). Further, extrinsic evidence may show that, due to a trade usage or custom (or even perhaps the parties' own private code), "black" means "white", "sell" means "buy" and vice versa, or "1,000" means "1,200"; see McLauchlan, "The Plain Meaning Rule of Contract Interpretation" (1996) 2 NZBLQ 80, 88-91.

Immediately after the passage quoted above, Hammond J continued:

> This is not the place to debate the recurrent controversy between the objective and subjective theories of assent to, or interpretation of a contract. It suffices to say that in this kind of case, the approach I have suggested may not always yield ideal justice; but it does yield a facility and certainty of interpretation which is preferable to that obtainable by looser approaches to interpretation. I have no doubt that the debate between stricter and looser standards of interpretation will roll down over the years, with proponents of one school or the other clutching at the latest appellate decision for such comfort as that may yield for the result desired for their particular interests. But, with respect, it is difficult to see why, in a genuine commercial agreement, the parties should be

able to say, "this is [now] what I thought I agreed to", rather than "this is how what I actually put my name to should be read".

This article too is not the place to debate the recurrent controversy, but two points should be noted. First, the so-called "looser standards" of interpretation are now enshrined in the New Zealand law concerning one important category of commercial contracts as a result of the recent implementation of the United Nations Convention on Contracts for the International Sale of Goods (see Art 8). Secondly, the last sentence in the above passage appears to exaggerate what divides proponents of "stricter and looser standards of interpretation". Not even the most liberal advocate of looser standards would suggest that a party to an interpretation dispute should be able to go into the witness box and, with the benefit of hindsight, simply say: "The interpretation I now contend is what I thought I agreed to". The position would be entirely different, however, if there were evidence of conduct or communications between the parties, whether before or after contract formation, which tended to support a conclusion that, at the time of the contract, the parties attached a particular meaning to the words in dispute, or at least that one of them did and the other knew or had reason to know of this meaning. (As to the admissibility of evidence of subsequent conduct, see McLauchlan, "Subsequent Conduct as an Aid to Interpretation" (1996) 2 NZBLQ 224.)

THE INTERPRETATION DISPUTE

Let us now turn to the details of the interpretation dispute. The written contract entered into by BP as seller and BA as buyer provided in cl 1, which unfortunately was not set out in the judgment, that "[e]xcept as otherwise provided in this Agreement, the Buyer agrees to purchase from the Seller and the Seller agrees to supply all the Buyer's requirements of the Petroleum Products for the Site and for the Term as specified in the First Schedule to this Agreement ... ". The term specified in the schedule was

> From: 1st day of December 1988
> To: 30th day of November 1993

However, cl 15.2 also provided:

> The Buyer shall be required to give the Seller 12 months notice in writing of its intention to terminate this Agreement on or after the due expiry date specified in the First Schedule.

In October 1994, some 10 months after expiry of "the term", BA advised BP that the agreement had been continuing on a month-to-month basis and gave 14 days' notice (later extended to one month). BP responded by claiming that cl 15.2 required 12 months' notice of BA's intention to terminate and that accordingly the agreement remained on foot until that notice had been given and the 12 months had expired. The parties were unable to resolve their dispute and eventually BP sought a declaration as to the proper interpretation of the termination provisions. The essential issue was whether BA was contractually obliged to give 12 months' notice when it decided to terminate the agreement in October 1994, thus extending the term to a period of six years 10 months.

Counsel for BP suggested that there were two possible interpretations of cl 15.2 and that, on either interpretation, 12 months' notice had to be given. Accordingly, BA could only terminate the agreement with effect from October 1995. The first interpretation was that the words "on or after the due expiry date" related to or qualified the words "intention to terminate" so that the *termination* had to be on or after the expiry date. Alternatively, "on or after... " related to the word "notice" so that the *notice* had to be given on or after the expiry date. However, the latter interpretation is unlikely to have been intended because it would have precluded the buyer giving a notice after four of the five years (ie 30 November 1992). Further, it was by inference rejected by the Judge. He thought (p 429) that the clause was silent on the point whether the notice had to be given "inside the primary term".

Counsel for BA argued, inter alia, that the agreement construed as a whole was for a fixed term of five years and hence came to an end on 30 November 1993. There could be no obligation to give 12 months' notice in October 1994 because the agreement had already expired. The problem with this interpretation was that it enabled BA to walk away from the contract immediately the five year term ended without giving any notice. It gave no effect at all to cl 15.2.

The writer's first impression on reading the contract was that there was no necessary inconsistency between the critical provisions and that, subject to the possibility of there being evidence of a contrary understanding concerning the effect of cl 15.2 at the time of the contract, BP's general contention was correct. This impression was partly based on two initial assumptions. First, parties to supply agreements in the petroleum industry would commonly fix a minimum term in the expectation that the arrangement would be rolled over until replaced by a new contract. Secondly, the seller might require a period of notice, regardless of whether the minimum term had expired, in order to give it the necessary time to arrange an alternative outlet for its brand of petrol in the district. Starting from these assumptions the provisions of the contract, though inelegantly drafted, seemed to fit together reasonably well. Thus, cl 1, which stated the primary obligations to sell and buy for the term specified in the first schedule, was made subject to the qualification "[e]xcept as otherwise provided in this Agreement". Clause 15.2 might fairly be seen as making provision for a possible extension to that term by requiring the buyer to give 12 months' notice of its intention to terminate the agreement "on or after the due expiry date", the intention being that the contract was to remain on foot in the meantime. As mentioned above, the natural interpretation of the words "on or after the due expiry date" is that they relate to termination not the giving of notice, otherwise the buyer would be precluded from giving notice to terminate at any time during the fifth year of the term. Thus, there could have been no objection to the buyer giving notice after, say, four and a half years to take effect 12 months later. By the same token, however, if the buyer resolved to terminate the agreement after it had operated for six or more years it would still be required to give the 12 months' notice.

The only real difficulty with this analysis is that the contract did not impose a reciprocal obligation on the seller to give notice. But it does not necessarily follow that the seller would have been entitled to terminate the agreement without notice immediately upon the expiration of the five year term. There would be a strong argument that the contract included an implied term obliging the seller to give reasonable notice.

THE JUDGE'S SOLUTION

The above interpretation, which is essentially an amplification of BP's reported argument, was rejected by Hammond J.

His Honour found that "[t]he objections to that approach must be at least threefold"(p 429). His first objection was that "such an approach isolates cl 15.2 from the rest of the agreement". This statement, for which no reason was given, is surprising. In the writer's view, the approach in fact does the opposite. It seeks to construe the contract as a whole and marry the allegedly inconsistent provisions in a manner that arguably makes commercial sense of the agreement. The second objection was that:

> the clause is actually silent on the particular point. It can surely be said that, on such a critical matter, the clause must be precise and that the Court should not have to guess at that which BP did not choose to plainly prescribe.

The "particular point" His Honour was referring to here is "does the notice have to be given inside the primary term?". He saw this as "the drafting deficiency". This too is surprising. In the writer's view, the main drafting deficiency was the failure to make the description of "the term" in the first schedule expressly subject to cl 15.2. If this had been done there would surely have been no difficulty. His Honour's "particular point" would not have arisen. Further, one would have thought that, in the context of a clause which at first sight required 12 months' notice to be given regardless of whether the primary term had expired, the fact that it was silent on the point whether the notice had to be given inside the term meant that the answer was no.

His Honour's final objection, in language reminiscent of that used by the famous American Judge and staunch objectivist Learned Hand J in *Eustis Mining Co v Beer, Sondheimer & Co* 239 F 976, 982 (1917), was as follows:

> Thirdly, there is always a critical breaking point beyond which language cannot be forced. There is routinely room for debate as to when that line, never quite a bright one, is reached. The argument here would be that to stretch the word "after" into a potentially infinite obligation, is to go too far.

For the reasons discussed in the article on the plain meaning rule referred to earlier, the writer cannot accept that there is any such "critical breaking point". In theory, language can be made to mean whatever the parties intend it to mean. But, that aside, it is difficult to see how BP's interpretation involved the imposition of "a potentially infinite obligation". BA simply had to give 12 months' notice once it had resolved to terminate the agreement.

After making the points discussed above, the Judge expressed his interpretation of cl 15.2 in the following passage (pp 429-430):

> The second broad approach is to treat cl 15.2 in the context of the agreement as a whole. That agreement, in the respects noted, does have a specific term. The words "or after" then make sense, as allowing 12 months' notice to be given within the term, but expiring outside it, for a maximum period of six years. For instance, notice could be given at four years to expire "on" the expiry date; and notice could even be given on the last day of the five years to expire one year later.

The result of this interpretation, which probably came as a surprise to counsel for both sides, was that, although BA had prematurely terminated the contract, "the greatest measure of protection BP could have had was up until the end of November 1994" (p 430). In other words, the maximum duration of the contract that BP could insist on was six years. Thus, in the particular circumstances that arose, BA was only obliged to give two months' notice. Further, if the facts had been that the parties had continued to operate under the agreement for a period of six years or more BA could have terminated at any time without giving notice pursuant to cl 15.2, which had ceased to apply.

THE CONTRA PROFERENTEM PRINCIPLE

A further interesting feature of Hammond J's reasoning is that he derived support for his conclusion from the contra proferentem principle of contract interpretation. His Honour said (p 430):

> Once there are two reasonably plausible meanings for the clause (as I think there are in this case) then the one which is less favourable to the party who supplied the language is to be preferred. This contra proferentem ("against the profferer") principle is much resorted to by Courts in disputes relating to standard-form contracts. And it has been particularly useful in relation to unequal bargaining situations (such as Draconian exemption clauses in consumer contracts). But I know of no authority, and I see no reason in principle, why it should not apply even between parties with equal bargaining strengths. I appreciate that at the end of the day, contra proferentem is really a rule of resolution, as opposed to something which can properly be said to be an intrinsic test assisting in the ascertaining of the meaning of something. Thus the benefit of the rule is functional rather than intrinsic; it is a tie-breaker, and penalises the careless drafter of documents. But the present case is a good illustration of the utility of the principle.

A number of points arise out of this analysis. First, on His Honour's version of contra proferentem, the principle will have limited application in the context of interpretation disputes involving commercial contracts. This is because both parties will commonly be involved in settling the terms of the contract. The final document will, to a greater or less extent, be the product of a joint effort. It would be surprising if His Honour considered it necessary in such circumstances to receive evidence concerning who was primarily responsible for the drafting of the provision in dispute.

Secondly, while it is true that in the *BP* case the contract was on the plaintiff's standard form and hence it was responsible for the document, it has to be questioned whether the approach to interpretation (and perhaps the result) should have been different if both sides had been involved in the drafting of the contract. Should it make such a difference that one side to a commercial transaction is content to accept the other's standard form, particularly if they are of equal bargaining strengths and each had access to legal advice? (Incidentally, at first sight it is surprising that the Judge should have regarded the parties before him as having equal bargaining strengths given the status and resources of BP. However, it may be that the imbalance in the latter respects was insignificant in the circumstances; for example, due to the competitive nature of the petrol industry at the time, BA may have been in a reasonably strong position to negotiate the terms. Further, the terms of the eventual contract were by no means one-sided.)

Thirdly, leaving aside the special position concerning exemption and limitation clauses (as well as perhaps insurance contracts), why should the presumption be that the "careless drafter" of a commercial contract between parties with equal bargaining strengths is to be penalised where

continued on p 444

TAXING PARTNERSHIPS: COGNATE ENTITIES

Tony Molloy QC

looks at the taxation of limited partnerships, joint ventures, syndicates, and "qualifying companies"

This article considers the fiscal ramifications of forms of unincorporated common enterprise other than partnerships such as special, or limited, partnerships; joint ventures; syndicates. It will also canvass recent reforms by which the tax system has, to a degree, assimilated the small company with the partnership.

INVESTMENT VEHICLE DRAWBACKS

When the top slice income tax rate approached 70 per cent in the 1980s, and while investment decisions were distorted by tax incentives enabling accelerated write offs against income which otherwise would have borne tax at that rate, schemes offering investments designed to provide write-offs to passive investors mushroomed.

If the scheme was so highly geared by contrived borrowing as to give rise to large losses, it was possible for investors to be allowed deductions which, when offset against income from other sources, could produce income tax savings several times greater than the amount of capital invested.

The prospect of entering into an ordinary partnership with promoters of these schemes was unlikely to be attractive to the ordinary investor with a defined amount to place at stake. The vulnerability of joint and several liability for losses was a major disincentive. Another drawback was the level of participation in the carrying on of the business which is of the essence of ordinary partnership. Most of those seeking tax shelter investments neither knew much about, nor wanted to be involved in running, schemes of the type offered.

The company, likewise, was a vehicle of limited value for these purposes. Its losses generally could not be shared for tax purposes with its non-corporate shareholders.

SPECIAL PARTNERSHIPS

Special partnership, or unlimited partnership, had been around for some time: see Molloy, "Unlimited Companies and Limited Partnerships in the Family Tax Plan" [1973] NZLJ 135. See also Webb and Molloy, *Principles of the Law of Partnership* (1996) Ch 7.

A defined amount could be invested. The special partners not only did not have to bother themselves with running the business, they were excluded from doing so. The losses were tax deductible, yet, subject to guarantees in respect of bona fide arm's length borrowing, the special partners were liable to no greater extent than their contributed capital.

Liability, but not deductibility, limited

Deductibility in respect of liabilities which truly had been incurred was not limited by the fact that, were the partnership to have been liquidated, the investor would have been liable to no greater extent than the capital she had agreed to contribute to the partnership.

Thus, although the liability of the taxpayer in *Reed v Young* [1986] 1 WLR 649; (1986) 59 TC 196 (HL), was limited to her contribution of £10,000, her £41,000 share in the loss of the limited partnership was tax deductible. She may not have had to contribute to the loss in that year, but she had to bear it in the sense that it would continue to be debited against the income of the firm in future years until, if ever, the venture should come into profit: (at 655; 228 per Lord Oliver of Aylmerton accepting a view which had been expressed by Dillon LJ in the Court of Appeal in the same case).

Lord Oliver, held, at p 654A; 227, that:

> [T]he partnership's trading losses are conceptually quite distinct from the debts and liabilities of the firm and from the assets which are available to meet them.

That potential abused

The fraudulent and shaky nature of large numbers of the special partnership schemes which were promoted in New Zealand during the 1980s made for great wastage of capital. They gave rise to a massive loss of tax revenue, with little or no countervailing benefit to the country.

The problem was widely replicated. In 1992 the Australian Parliament moved to check it by inserting into the Income Tax Assessment Act 1936 a new Subdivision C of Division 5A of Part III. This Subdivision effectively deemed limited partnerships to be companies for almost every fiscal purpose. Two critical exceptions were that, by s 94V(1):

(b) the partners are jointly and severally liable to pay any amount [of income tax] that would be payable by the partnership;

(c) any offence against the income tax law that would otherwise be committed by the partnership is taken to have been committed by each of the partners.

The defence against para (c), provided by subs (2), was open only to the partner able to prove that she had neither aided nor abetted nor, directly or indirectly and whether by act or omission, been knowingly concerned in the actus reus.

Legislative response: losses quarantined

In the meantime, the New Zealand Parliament had moved to put special partnership tax losses into quarantine. What is now s HC 1 Income Tax Act 1994 was enacted in 1986.

Subsections (1) to (4) provided that losses incurred by any special partnership registered after 1 August 1986, or raising capital after that date save pursuant to a pre-existing commitment, could not be offset against other income of the partners save any income which the partnership might derive in future years.

By subs (11), partnerships registered prior to that date, may continue to be treated as outside s HC 1 once they have been continued or renewed.

As well as being quarantined, any loss which had been based on any debt will cease to be available, for offset against future income, to the extent to which, in the meantime, it may have become remitted or cancelled by affluxion of time, insolvency, composition with creditors, or otherwise without fully adequate consideration: subss (7), (9).

Any quarantined loss also will be exterminated for carry-forward purposes where, if the partnership had been a company, the shares in which were owned in the proportions in which the partners owned the certified capital of the special partnership, the carry forward of the loss would have been precluded by ss IE 1 and IF 1. IE 1(b) limits the circumstances in which such losses could be carried forward

> to those where the tax benefit arising from the set off is obtained (directly or indirectly), at least to the extent of 49 per cent, only by the same natural persons holding (directly or indirectly) rights in relation to the company who, by virtue of holding such rights, effectively bore the loss.

The Final Report of the Consultative Committee on the Taxation of Income from Capital, released in October 1992, considered, but rejected, possible assimilation of the positions of the special partnership and of the loss attributing qualifying company. At para 5.10, the Report found:

> We consider that a special partnership is generally a surrogate for a widely-held company and does not have the same characteristics as those required for a loss attributing qualifying company. We are unable to recommend that the existing prohibition on the flow through of losses to the special partners in a special partnership be removed but believe that the status of special partnerships should be examined as part of the recommended comprehensive review, particularly to ensure that there is a consistent approach for economically equivalent entities.

COGNATE REFORMS

Small companies and partnerships

The notion of treating the firm as a full entity has been considered for some time. So far as small companies are concerned, something like that notion is to be found in the elective "qualifying company" regime which became effective during fiscal 1993. It was introduced on the recommendation of the November 1990 and July 1991 reports on *The Taxation of Distributions from Companies* by the Consultative Committee on the Taxation of Income from Capital.

Subpart G of Part H of the Income Tax Act 1994 details the regime on the basis of the position stated in s HG 1:

> Subject to the express provisions of this Subpart, any company that
>
> (a) Is owned by 5 or fewer natural persons as counted in accordance with s OB 3; or
>
> (b) Is a flat-owning company within the meaning of subs (1)(b)(ii) of that section –
>
> and that otherwise meets the requirements of that section may, by making the appropriate elections,
>
> (c) Make distributions to its shareholders of its gains in such a fashion that the distributed gains are subjected to taxation; and
>
> (d) Where the company has only one class of shares, allocate its losses to its shareholders in such a fashion that the losses are dealt with for taxation purposes, in like manner to that which would have occurred had the company been a partnership

This measure goes some way towards removing the economic differences between the partnership or corporate options open to the small New Zealand resident firm. However the legal steps are quite different. The income of a partnership is not taxed to the firm at all, but only to the partners to whom it has been allocated; and then only in accord with their respective overall fiscal situations.

The qualifying company, on the other hand, as defined by s OB3, is taxed on its income like any other company. However, the shareholders are personally liable for a percentage of the tax payable by the company: s HG 4.

The partnership can retain any of its gains, or pass them to its members. Because the firm is not taxed itself, it is able to distribute the entirety of the gains, and not just the tax paid balance of them.

On the other hand, because the qualifying company is taxed, it may retain no more than the tax paid balance of its profits. Or it may distribute that balance by way of dividends which carry full imputation credits, or are exempt: and, either way, effectively will be tax free (including resident withholding tax free: s HG 13(1)(a)) in the hands of its New Zealand resident shareholders: s HG 13(2)-(6). Or the company may partially retain and partially distribute.

The partnership is restricted in deducting salaries paid to its partners save in the circumstances discussed in the article at [1996] NZLJ 345.

The qualifying company, on the other hand, can pay salaries to its shareholder/employees; can deduct them for income tax purposes; and can in that way distribute the whole of its income just like a partnership. This ability remains limited by the considerations affecting "salaries" which really are dividends: *Aspro Ltd v Commissioner of Taxes* [1932] AC 583; (1932) NZPCC 630. See *Molloy On Income Tax* (1976) 302-303.

Finally, losses made by the partnership are passed on automatically to the members of the firm. A qualifying company, the members of which elect that it shall be a "loss attributing qualifying company" (s HG 14), likewise can pass its losses directly to its members in proportion to their respective effective interests in the company: s HG 16.

JOINT VENTURES

Joint venture is another concept associated with the partnership: see Webb and Molloy, *Principles of the Law of Partnership* (1996) Chapter 10; McInnes, "Joint Ventures: Status Vis-a-Vis Third Parties and the Commissioner of Inland Revenue" in Prebble (ed), *Dimensions in Business Finance Law* (1992) 177-196; Doran, *Taxation of Corporate Joint Ventures* (1993).

In the tax context, it has been described in the US Tax Court, in *Podell v CIR* (1970) 55 TC 429 as an arrangement providing for the establishment and control of a business venture; for the contribution of the money, property or services of the joint venturers; and for the sharing of profits although not necessarily of losses. The venture found to exist in that case was between a lawyer who agreed to advance money to a developer, and the developer who used the money in the buying, renovating and reselling of real property. The parties shared the profits.

Harley v CIR [1971] NZLR 482 was a case where, within this description, the arrangement provided for "the contribution of the ... property" of the parties towards their joint venture: See *Molloy on Income Tax* (1976) 311-312.

The property contributed was the adjacent smallholding of each of the parties. The arrangement was that the parties would graze the properties as one farm while each would remain responsible for the outgoings in respect of their own block. Although content to deal with the case as one of partnership, because that is how it had been argued and because there was no fiscal significance in the difference, Turner J noted, [1971] NZLR 482, 491-492, that, like North P, he would have been inclined to treat the parties' relationship "rather as a venture of co-owners than as a partnership in the strict sense".

Joint ventures and the tax system

The Goods and Services Tax Act 1985 expressly includes "joint venture", along with partnership and trusteeship, as "unincorporated bodies of persons" capable of becoming "registered persons". The legislation otherwise does not mention the concept.

Apart from a single enactment, s OC 1, relating to the taxation of airport operators, for the purposes of which there is a definition in s OB 1 of "joint venture agreement", the Income Tax Act 1994 likewise gives no express recognition to joint ventures as such.

For GST purposes there is no significance in the distinction between joint venture and partnership.

Apart from airport operators, the only relevance of distinguishing between joint venture and partnership for income tax purposes is that a partnership must file a joint return (Tax Administration Act 1994 s 42(1)(b)(i)), whereas a joint venture need not: s 42(1)(c).

SYNDICATES

Property owning syndicates once were the bane of legislators intent on maintaining the double taxation of income as it was derived by a company and as it was later distributed to the shareholders. To avoid loss of this double source of revenue when groups of property investors pooled their resources other than by means of incorporation of a company, legislation was enacted which aimed at "any unincorporated association comprising members not less than 11 in number ... engaged, whether as a partnership ... or otherwise howsoever ... in the activities of ... acquiring or holding any real property". Enacted by s 25(1) of the Land and Income Tax Amendment Act 1971, as Land and Income Tax Act 1954 s 153BB, and repealed by Income Tax Amendment Act 1980 s 42(1) when it was Income Tax Act 1976 s 212, this provision declared any such association to be a "syndicate" and subjected it to the like taxation regime as if it were to have been a company.

While it is clear that a partnership would have been possessed of the element of "association" essential to "syndicate" status for this purpose; it was equally clear that mere co-ownership of property, in the absence of mutual rights and obligations, did not possess that element: *Taunton Syndicate v CIR* (1982) 5 TRNZ 259; (1982) 5 NZTC 61,106.

Although the taxpayers in that case were not in partnership, and their use of the name "syndicate" did not make them a partnership, it is clear that adoption of the name "syndicate" by a partnership will not be effective to transmute it into something which is not a partnership: *Sarich v FCT* (1978) 9 ATR 29 ❑

---

continued from p441

there are two reasonably plausible meanings for a particular term? Let us assume that there is no reliable evidence that the parties attached a particular meaning to the term at the time of the contract (or that one of them did and the other knew or had reason to know of this meaning). Should not the whole focU of the Court's inquiry be to determine which interpretation is more reasonable in the light of the object of the transaction and the other surrounding circumstances? Or, in other words, which interpretation makes most commercial sense and is thus likely to reflect the reasonable expectations of the parties to the transaction? If, as is generally accepted, the Courts should "seek to uphold bargains made between businessmen wherever possible, recognising that they often record the most important agreements in crude and summary fashion" (9 *Halsbury's Laws of England*, 4 ed, para 269), why should the position be different, and the careless drafter (whoever that happens to be) penalised, where there is an interpretation as opposed to a formation dispute?

Fourthly, and most importantly, Hammond J's version of the contra proferentem principle would not command universal agreement. He says that the principle means that the interpretation which is less favourable to the party who supplied the language or drafted the contract is to be preferred. Another view is that the interpretation to be preferred is that which is less favourable to the party for whose benefit the term is included and who is seeking to invoke its protection. On this view,

> identification of the *proferens* should not be confused with identification of the draftsman .... The true principle is that the *proferens* is the person for whose benefit the clause was inserted rather than the person who actually did the drafting. (Lewison, *The Interpretation of Contracts*, 1989, pp 136-137)

Thus, contra proferentem might well apply where both sides have an input to the drafting of the contract. Indeed, "[e]ach party to a contract may be a *proferens* in respect of different parts of it" (*Lewison*, supra, at p 136).

Finally, as Hammond J stressed, in the context of commercial agreements the contra proferentem principle is in the nature of a tie-breaker rather than "an intrinsic test assisting in the ascertaining of the meaning of something" (p 430). In other words, the principle is to be invoked when the usual rules of interpretation fail and no satisfactory basis for preferring one meaning over another can be found. The irony of this is that His Honour had earlier observed, in rejecting extrinsic aids to interpretation, that this contract had "its own meaning". In addition, he expressed a preference for the "traditional approach" to issues of interpretation because it has the advantage of yielding "a facility and certainty of interpretation which is preferable to that obtainable by looser standards of interpretation"(p 429). But who would have predicted the interpretation favoured by the Judge on this occasion? And who would be prepared to predict the outcome if an appeal were to proceed? ❑

DISSOLVING PARTNERSHIPS: "JUST AND EQUITABLE"

P R H Webb, Emeritus Professor of Law, University of Auckland

considers the dissolution of partnerships on the "just and equitable" ground

Section 38(f) Partnership Act 1908 gives the Court a discretion to dissolve a partnership whenever circumstances have arisen which, in the opinion of the Court, render it just and equitable that the partnership should be dissolved. The provision does not explicitly state that the partner suing is required to be faultless; it does not require that he or she must come to Court with "squeaky clean" hands (s 38(b) – (d)), which expressly exclude as plaintiff a partner who is in the wrong. It was made clear, however, in *Ebrahimi v Westbourne Galleries Ltd* (see, eg [1973] AC 370 (HL) at 387, per Lord Cross of Chelsea. that an application would not be granted if made by a partner whose conduct was the sole cause of dissension in the firm.

In the light of the above, two recent Canadian and Australian cases call for comment. The first is *Landford Greens Ltd v 746370 Ontario Inc* (1994) 12 BLR (2d) 196, where 746370 Ontario Inc (746370 Inc) had entered into a partnership agreement with Landford Greens Ltd (LG Ltd) to construct, operate and lease four office block buildings. 746370 Inc had contributed the land and LG Ltd was to pay 746370 Inc half the value of it in three instalments, arrange the finance and operate the buildings. 746370 Inc was not required to contribute further finance. Unfortunately, shortly after the formation of the partnership the commercial real estate market plummeted. This had the effect of forcing the partners to decide to build only one building, which would be marketed as a condominium.

LG Ltd did not pay the third instalment, and so might be viewed as being the defaulting partner. 746370 Inc, as it was entitled to do under the terms of the partnership agreement, attempted to buy out LG Ltd's interest. 746370 Inc was unable to obtain releases of LG Ltd's guarantees and the purchase was accordingly not concluded.

LG Ltd thereupon sought, but without success, to have the partnership dissolved on the grounds first that it had been entered into for a single undertaking which had been terminated (s 35(1)(b) Partnership Act 1908), and secondly that the partnership's business could only be carried on at a loss. (s 38(e)) The first ground failed for lack of evidence that the purpose for which the partnership had been created had become impossible to perform; while market conditions had caused the change of the business plan, they had not rendered the partnership business impossible. The second ground failed for lack of evidence that the business could not ever be profitable (see *Handyside v Campbell* (1901) 17 TLR 623 with *Janson v McMullen* [1922] NZLR 677).

LG Ltd's main ground for seeking dissolution, however, was that it would be just and equitable that the partnership be wound up. It argued that their dispute over funding demonstrated a lack of trust between it and 746370 Inc and that it was still incurring expenses on the partnership's behalf, thus carrying 746370 Inc's investment. 746370 Inc's counter-argument was that it would be inequitable for dissolution to be ordered because it would lose the value of its investment and LG Ltd would be freed from the obligations which it had agreed to undertake.

Ground J held that there had to be such a complete breakdown of mutual trust and confidence as would preclude all hope of reconciliation and future cooperation, ie it had to be shown that it was impossible for the partners to place that confidence in each other which each had the right to expect. Such impossibility, it was emphasised, must not have been caused by the partner seeking to take advantage of it. In the present case, Ground J found, there was not a deadlock or, even, a substantial disagreement on questions of the day-to-day management of the operation. Management of the operation was in LG Ltd's hands, and there was no such lack of confidence or trust between the partners as to render it virtually impossible for them to continue in business together as partners. LG Ltd's application was accordingly dismissed outright with costs to 746370 Inc on a party and party basis. (See (1994) 12 BLR (2d) at 205-208.)

It is instructive to compare the approach taken by Santow J in *Ruut v Head* (1996) 20 ACSR 160. The parties were partners in a radiology practice. Dr Ruut (R) excluded Dr Head (H) from the partnership, which brought about a breakdown in their relationship, and applied to have the partnership wound up on the just and equitable ground. R subsequently conceded that his exclusion of H had been wrongful. Not unnaturally, H argued that R was precluded from obtaining the order he sought by reason of his lack of clean hands. Santown J expressed himself as

> not satisfied that the continuance of the partnership for any length of time would be a sensible course as I consider that the relations between the parties and their mutual trust and confidence have irretrievably broken down as conceded by [H] .... In short, I am satisfied that not only had [R] played a material role in [the] breakdown but that [R's] wrongful exclusion of [H] was the predominant cause of that breakdown. None of the factual matters advanced by [R] as attributing partial responsibility to [H] go far enough to alter that result. It has been agreed by the parties that I need not give any detailed reasons for that conclusion. (at 160-161)

It must be explained that the partnership agreement provided that a partner seeking to wind up could withdraw from the partnership and be bought out by the other partner at a fair price if that other so elected, and that, upon failure to elect, the partnership could be wound up. This was, however, conceded to be subject to the Court's overriding discretion to deal with the matter under the just and equitable ground. Neither R nor H had yet triggered the provision as to withdrawal. (Cf *Re American Pioneer Leather Co Ltd* [1918] 1 Ch 557, where the option to buy out had, in fact, been passed up by the party entitled to purchase.)

His Honour stated (at 162):

> Thus there may be circumstances where the conduct of the party seeking winding up is such that the Court, in all the circumstances, is not minded to wind up the partnership, even though trust has broken down irretrievably. The partners may be still short of absolute deadlock, or one partner may be wholly at fault and has contrived the breakdown. Thus in *Re Yenidje Tobacco Company* [[1916] 2 Ch 426 (CA) at 430, a seminal decision in the present context] ... there was a complete breakdown of relations. The Court (in dicta) suggested that the impossibility of partners placing confidence in each other, relied on for winding up, must not be caused by the partner seeking to take advantage of it by winding up.

After considering *Yenidje*, he went on to say (at 162-163):

> As a matter of logic, lack of clean hands could not be an absolute bar, else otherwise for example, where both partners are equally at fault, neither could obtain a winding up order. Nonetheless it must be an important factor in the exercise of the Court's discretion along with other factors, such as whether the partnership was truly deadlocked.
>
> In the events that happened in *Re Yenidje*. It was evidently not the case that the impossibility of the partners placing confidence in each other was caused by the partner seeking to take advantage of it, given that the winding up order was made. That is a difference with the present situation before me. A partnership like the present may limp along though probably for a relatively short time, despite being irretrievably broken down. This is because it is not so deadlocked that there is necessarily lacking the minimal co-operation needed to bring it to an end consensually. This may be either by one partner withdrawing and the other buying him out, or by an agreement sale of the partnership business with proceeds then divided up, even if neither outcome is certain to follow. Mutual self-interest in achieving a consensual end may still suffice to bring that about, despite acrimony or lack of trust.
>
> In the present circumstances, there are thus several factors pointing against winding up the partnership, namely [R's] lack of clean hands, [R's] opportunity to extricate himself from the partnership by invoking [the provisions in the partnership agreement adverted to above] without need for a winding up order at this point and the fact that there may not be a complete deadlock preventing a consensual termination. The Court should not lend itself to winding up a partnership too readily or too quickly, where only one partner has brought about the breakdown of relations and might thereby profit from his own wrong.
>
> On the other hand there is the fact that the relations between the partners have irretrievably broken down. There may even be a public interest in not allowing partnerships providing important services to the public to continue to trade, or practise a profession, where their partners are simply unable to work together.

there may even be a public interest in not allowing partnerships providing important services to the public to continue to trade, or practise a profession, where their partners are simply unable to work together.

Having said this, Santow J did not proceed to refuse to order dissolution outright. He made it clear that the case was to come back before him in three months' time when, in the light of the circumstances prevailing at that time, he would consider whether or not to make a dissolution order. This course would give either party the chance to buy the other out and also afford an opportunity for the business to be sold (as was presently sought by R) advantageously and without the "distress factor of a winding up order operating to the detriment of both parties". After observing that the partnership was still a profitable one and was not necessarily totally deadlocked, the Court stated its preference for this course rather than making a dissolution order but deferring it application for three months or so. The "distress factor" on the sale price would be avoided and there possibly would be a greater incentive for the parties to work out some acceptable alternative (at 163).

> This includes, being bought out ... or selling to a third party, or both, knowing that there is a sword of Damocles hanging over the parties in three months time if they are unable to reach a sensible consensual resolution with the minimal co-operation necessary to do so. (ibid).

It is submitted that this decision exemplified nicely a suitable via media between an out-and-out refusal of a dissolution order and ordering an immediate dissolution but deferring its operation for a given period. Courts appear, though, for the purpose of exercising their discretion, to be required to decide in any given case whether the partner suing is 100 per cent "squeaky clean", is exactly and precisely in pari delicto with his or her other partner or partners, is 100 per cent to blame (presumably the defendant partner in *Phillips v Melville* [1921] NZLR 571 can be taken to have been 100 per cent to blame for the parties' breakdown and would not have been granted a dissolution order under this head had he been the plaintiff in those proceedings) (and so is the sole cause of the breakdown) or is, for example, as much as 75 per cent (and so predominantly) to blame or, for that matter, only 40 per cent (and so not principally) to blame. Is it desirable too for the Courts to feel compelled to proceed on the same kind of basis as they have to do when considering the possibility of a plaintiff's contributory negligence?

GENERAL REFERENCES

For general discussion of the just and equitable ground, see Lindley & Banks on Partnerships (17 ed, 1995), paras 24-75 – 24-76, together with paras 24-66 – 24-72; Webb & Molloy, *Principles of the Law of Partnership* (6th ed, 1996), para 5.137 and Higgins & Fletcher, *The Law of Partnership in Australia and New Zealand* (7th ed, 1995), at 224-227). ❑

EQUITY, RESTITUTION AND COMMERCIAL COMMON SENSE

David Friar, Kensington Swan, Wellington

analyses a recent House of Lords case which considered the relationship between equity and restitution

The House of Lords case of *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] 2 All ER 961 is a significant decision in the developing law of restitution. The majority of Their Lordships affirmed traditional equitable doctrines, and rejected an all-encompassing law of restitution. They also counselled against the importation into commercial law of equitable principles inconsistent with commercial certainty.

BACKGROUND

The parties entered an interest rate swap agreement in 1987. This was in substance a loan. The bank paid the council £2.5 million in 1987 and, for the following ten years, they were each to make interest payments to the other on a notional principal of £25 million. The bank was to pay interest to the council at 7.5 per cent per annum. The council was to pay interest to the bank at a fluctuating rate, which averaged 10.2 per cent per annum. In reality, the council paid the bank the net difference of 2.7 per cent per annum.

In 1989, interest rate swap agreements were held to be ultra vires local authorities. Because the agreement was void ab initio, the bank claimed it was entitled to be restored to the position it was in before the agreement was entered. It claimed the £2.5 million it had paid in 1987, less the net interest of £1.35 million the council had paid the bank.

It was accepted by both parties that the bank had a common law right in restitution to the money. The bank also claimed compound interest on the money from 1987. The minority (Lords Goff and Woolf) held that the Court had jurisdiction to award compound interest on a common law claim. Despite the traditional rule that compound interest could only be awarded in equity, Lord Goff said at 981:

> ... the warm sun of judicial creativity should exercise its benign influence rather than remain hidden behind the dark clouds of judicial history.

The majority rejected this. Lords Browne-Wilkinson, Slynn and Lloyd upheld the traditional position that compound interest could only be awarded in equity. They held that although the bank had a strong moral claim to compound interest, it was for Parliament and not the Courts to make any changes to the existing law. Because it sought compound interest, the bank therefore claimed an equitable proprietary interest in the money.

THE ISSUES

Their Lordships considered a range of issues in equity, restitution and commercial law. This article focuses on the two principal issues. The first is the nature and extent of equitable proprietary interests; the second issue is the nature and ambit of the law of trusts.

These two topics must be considered in their broader context, and in particular the debate between equity and restitution lawyers. Should equitable proprietary interests be premised on the unjust enrichment of a defendant, or on an existing equitable relationship between the defendant and the plaintiff? If an equitable relationship such as a trust is required, can a trust arise on the basis of the defendant's unjust enrichment? Or can a trust only arise according to traditional equitable principles?

A further question is the relationship between equity and restitution on the one hand and commercial law on the other. To what extent should equitable principles be introduced into commercial law? And to what extent should the Courts allow proprietary interests to interfere with commercial dealings?

EQUITABLE PROPRIETARY INTERESTS

As well as enabling the plaintiff to claim compound interest, an equitable proprietary interest has three general advantages over a personal right at common law:

- if the defendant is insolvent, the plaintiff has a better right to the money than the defendant's creditors;
- if the original recipient transfers the money to a third party who is not a bona fide purchaser for value, the plaintiff's interest is enforceable against that third party; and
- the plaintiff has a right to any profits made from the property

The law of equitable proprietary interests is an area in which no coherent approach has yet been adopted. Indeed, Lord Goff stated at 969 that "the role of equitable proprietary claims in the law of restitution has been found to be a matter of great difficulty".

The source of this difficulty may be traced back to the House of Lords decision of *Sinclair v Brougham* [1914] AC 398. The decision was described as a "bewildering authority" by Lord Browne-Wilkinson at 996 in the present case, and with speeches "not only difficult to follow but difficult to reconcile with one another" by the English Court of Appeal in *Re Diplock's Estate* [1948] Ch 465, 518.

Equity: the traditional test

Traditionally, an equitable proprietary interest could only arise in the context of a fiduciary relationship. It was this "prism" of a fiduciary relationship that split the legal from the equitable entitlement. Unless a plaintiff could show a subsisting fiduciary relationship, the plaintiff could not claim an equitable proprietary interest in any money received by the defendant.

Trusts and other fiduciary relationships were subject to equitable proprietary claims; normal commercial dealings were not. The far-reaching consequences of equitable proprietary claims were thus limited by the narrow class of relationships subject to such claims.

Restitution: a new test?

More recently, this requirement has been challenged by a number of restitution lawyers. Professor Birks argues in *An Introduction to the Law of Restitution* (1989) at pp 378-385 that a plaintiff can claim an equitable proprietary interest irrespective of any subsisting fiduciary relationship. An equitable proprietary claim can be made by a plaintiff who at the time the money is passed to the recipient either retains or obtains an equitable proprietary interest. If the nature of the transaction is such that the plaintiff does retain or obtain such an interest, then the plaintiff has a sufficient proprietary base to make an equitable proprietary claim.

This can happen consensually. When a trust is settled, for example, the beneficiaries obtain an equitable proprietary interest in the trust property.

This can also happen by operation of law. An example of this is the recent High Court case of *Hongkong and Shanghai Banking Corporation Ltd v Fortex Group Ltd* (1995) 5 NZBLC 103,869. The bank paid Fortex US$340,000 under a mistake of fact. Master Hansen held that because of the mistake, the bank retained an equitable proprietary interest in the money. Although there was no fiduciary relationship between the bank and Fortex, the mistake was itself sufficient to trigger an equitable proprietary interest.

According to restitution lawyers, the plaintiff has a sufficient proprietary base to claim an equitable proprietary interest if the defendant has been "unjustly" enriched at the plaintiff's expense. "Unjust" here does not mean that the transaction offends against a Judge's sense of fairness. Nor does it mean a transaction that would result in a personal restitutionary claim. Rather, it refers to a number of specific types of transaction that trigger an equitable proprietary interest. In *Fortex* it was the mistake that was the unjust factor. Goff & Jones at p 94 of *The Law of Restitution* (4th ed 1993) suggest the following further "unjust" factors:

> A person who confers a benefit, normally a money payment, under mistake, compulsion, necessity or in consequence of another's wrongful or unconscionable conduct will be *deemed* to have retained the equitable title in the money paid.

What then of the traditional requirement of a fiduciary relationship? Birks explains this away by arguing that such a relationship is not a requirement but a consequence of finding an equitable proprietary interest. Although a fiduciary relationship will therefore always be present, the touchstone is whether the plaintiff obtains or retains such an interest. This was accepted by Master Hansen in the *Fortex* case at 103,877:

> It is apparent ... that it is the payment by mistake that creates the fiduciary obligation, and brings the fiduciary relationship into existence.

Their Lordships' response

The bank argued that although legal title to the money passed to the bank, the fact that the agreement was void meant that the bank retained an equitable title to the money. Lord Browne-Wilkinson (Lords Woolf, Slynn and Lloyd agreeing) rejected this argument, holding that it was not possible to *retain* an equitable interest. He said at 989:

> I think this argument is fallacious. A person solely entitled to the full beneficial ownership of money or property, both at law or in equity, does not enjoy an equitable interest in that property. The legal title carries with it all rights. Unless and until there is a separation of the legal and equitable estates, there is no separate title. Therefore to talk about the bank "retaining" its equitable interest is meaningless.

Did the bank obtain an equitable proprietary interest because of the void agreement? No. Lord Browne-Wilkinson held that such an interest cannot arise from the unjust enrichment of a defendant such as a mistaken payment or a void agreement. An equitable proprietary interest can only arise under a trust or other fiduciary relationship. He said at 989:

> The only question is whether the circumstances under which the money was paid were such as, in equity, to impose a trust on the local authority. If so, an equitable interest arose for the first time under that trust.

This would seem to be a clear rejection of Birks' argument. If an equitable proprietary interest only arises under a trust or other fiduciary relationship, there would seem to be no place for unjust enrichment. The question is whether the parties are subject to a trust, and not whether the defendant has been unjustly enriched.

However, to hold that an equitable proprietary interest can only arise under a trust does not take us much further. When does a trust arise? If a trust can be created on the basis of an unjust enrichment, then an equitable proprietary interest can still arise on the basis of the defendant's unjust enrichment, albeit through the indirect route of trust law. Although Lord Browne-Wilkinson rejected the plaintiff's ability to retain an equitable proprietary interest on the basis of an unjust enrichment, his analysis of the law of trusts may mean that the defendant's unjust enrichment is still relevant.

THE LAW OF TRUSTS

The basis on which trusts arise has been debated for some time. This is particularly so for non-express trusts. In the present case, Lord Browne-Wilkinson develops a general theory of trust law, encompassing both express and non-express trusts. He outlines at 988 two of the essential requirements for a trust to arise:

- there must be defined trust property; and
- the conscience of the owner of the legal interest in relation to this property is affected

What is meant by the "conscience" of the legal owner being "affected"? This is simply a reference to knowledge. A person who holds legal title to property cannot be a trustee of that property unless she or he *knows* of the facts alleged to give rise to the trust. Thus in the case of an express trust, the legal owner must know that she or he is intended to hold the property for the benefit of others. And in the case of a non-express trust (a resulting or constructive trust), the owner of the legal interest must know of the circumstances giving rise to the trust.

Despite Lord Browne-Wilkinson labelling these propositions as fundamental and uncontroversial, knowledge on the part of the legal owner has not previously been considered a requirement for a trust to arise. But we should be clear on the role knowledge (or "affected conscience") plays in his Lordship's theory. This requirement does not mean that trusts can only arise if consistent with good conscience; it means that they can only arise if the legal owner knows the facts alleged to give rise to the trust. Nor is the requirement intended to replace the existing rules determining the existence of a trust. Rather, it is an additional requirement. Finally, it will not increase the incidence of trusts. Because it is additional, it will reduce the situations in which a trust arises (for a different view as to the consequences of this requirement, see Rickett, "Developments in the Law of Obligations", NZLS Seminar November 1996, p 31).

This additional requirement adds little to the existing requirements for express trusts. Because they only arise by the consent of the parties, the holder of the legal interest will always know that she or he is intended to hold the property for the benefit of others. However, the requirement of knowledge is a significant addition to the requirements for non-express trusts.

Resulting trusts

A resulting trust gives effect to the presumed intentions of the parties. A resulting trust traditionally arises in two circumstances. The first is where A apparently gifts property to B. It is presumed that A did not intend to make a gift, and the property is held on a resulting trust for A. The second is where A transfers property to B on an express trust, but the equitable interest is not completely disposed of. Again, that interest is held on trust for A. In both cases, B must be aware of the circumstances giving rise to the presumed intention before a trust arises.

Birks argues in "Restitution and Resulting Trusts" (in *Equity and Contemporary Legal Developments* 335 at 360) that a resulting trust should also be found in situations where A has transferred value to B under a mistake or under a contract the consideration for which has wholly failed. He argues that the resulting trust comes into play whenever it appears that A did not intend to benefit B. Because A does not intend to benefit B if value is transferred under a mistake or failure of consideration, the value received by B should be held for A on a resulting trust.

This was unanimously rejected by their Lordships. Whatever intellectual merit his case may have, they considered the consequences of such an extension unwarranted. They restricted the resulting trust to the traditional categories. Lord Browne-Wilkinson said at 992:

> I do not think it right to make an unprincipled alteration to the law of property (ie the law of trusts) so as to produce in the law of unjust enrichment the injustices to third parties which I have mentioned and the consequential commercial uncertainty which any extension of proprietary interests in personal property is bound to produce.

Institutional constructive trusts

An institutional constructive trust arises not on the basis of the parties' intentions, but is imposed by the Court on the recipient by reason of his or her unconscionable conduct. It arises not when declared by the Court, but when the recipient becomes aware of the facts which give rise to the trust. This is why it is considered "institutional": it arises independently of any Court order.

Lord Browne-Wilkinson did not directly address the type of unconscionable conduct sufficient to give rise to an institutional constructive trust. However, he referred to *Metall and Rohstoff AG v Donaldson Lufkin & Jenrette* [1989] 3 ALL ER 14 at 53, in which the English Court of Appeal outlined three situations in which an institutional constructive trust arises.

In the first, where a person receives property already subject to a trust with actual or constructive notice that it is trust property and that the transfer is in breach of trust ("knowing receipt"). The second situation is where a person acquires notice of the trust after receiving the trust property and then deals with it in a manner inconsistent with the trust ("wrongful dealing"). The third is where a person who while not actually receiving any trust property dishonestly assists in the breach of a trust ("dishonest assistance").

There is a further situation in which a institutional constructive trust arises. A trustee (or other fiduciary) who profits from the trust holds such a profit on a constructive trust. For example, where a trustee receives an improper commission, or uses information acquired as a trustee to make a profit, that commission or profit is held on an institutional constructive trust.

For each type of institutional constructive trust, the conduct of the defendant occurs against the background of a pre-existing trust or fiduciary relationship. The two exceptions to this are the constructive trusts that arise when a contract for the sale of land is entered, and mutual wills. Apart from these cases, a claim for an institutional constructive trust must occur against the backdrop of a trust or other fiduciary relationship. An institutional constructive trust does not arise on the basis of an unjust enrichment.

Remedial constructive trusts

In contrast to the institutional constructive trust, this is a judicial remedy giving rise to an enforceable equitable obligation. The remedial constructive trust only arises by order of the Court, and the extent to which it operates lies in the discretion of the Court.

Lord Browne-Wilkinson did not decide whether English law should adopt the remedial constructive trust. However, he did give some indication as to the basis for imposing such a trust. He said at 999:

> The Court by way of remedy might impose a constructive trust on a defendant who knowingly retains property of which the plaintiff has been unjustly deprived. Since the remedy can be tailored to the circumstances of the particular case, innocent third parties would not be prejudiced ...

On his Lordship's analysis, the remedial constructive trust is premised on the defendant's unjust enrichment. If the defendant has been unjustly enriched by a subtraction of value from the plaintiff, and the defendant knows this (ie has an "affected conscience"), then the Courts may impose a remedial constructive trust. However, a plaintiff who is awarded a remedial constructive trust does not necessarily also acquire the benefits of the equitable proprietary interest that accompanies a trust. Because this trust is remedial, the Court can tailor the consequences of awarding an equitable proprietary interest to the circumstances of particular cases.

The remedial constructive trust has been accepted in a commercial context by the New Zealand Court of Appeal, albeit premised on a different basis than unjust enrichment. In *Elders Pastoral v BNZ* [1989] 2 NZLR 180, Cooke P awarded a remedial constructive trust on the basis of the reasonable expectations of the parties. And in *Liggett v Kensington* [1993] 1 NZLR 257, Gault J considered a number of factors in determining whether there was a remedial constructive trust. It remains to be seen whether the New Zealand Courts will continue these "reasonable expectations" or factors-based tests, or whether they will premise the remedial constructive trust on the unjust enrichment of the defendant.

The bank's argument

There was clearly no express trust between the bank and the council. Nor could the bank argue that there was a resulting trust, given the restrictive definition adopted by their Lordships. And the bank could not claim a constructive trust, institutional or remedial. The council had no knowledge sufficient to raise a constructive trust at any time before the money became untraceable. Therefore the council did not hold the money on trust for the bank, and the bank thus did not have an equitable proprietary interest in the money.

ANALYSIS

Few would deny that a personal remedy in restitution should be available where a defendant has been unjustly enriched at the plaintiff's expense. The issue, however, is whether the benefits of an equitable proprietary interest should be available to the plaintiff. Whether an equitable proprietary interest arises directly from the defendant's unjust enrichment, or indirectly by means of a trust raised on the basis of the defendant's unjust enrichment, such an interest entails far-reaching consequences. Although in some circumstances these consequences may be defensible, in other cases they simply cannot be justified.

One consequence of bringing a proprietary claim is that the plaintiff can recover any profits made by the defendant. If the defendant knew of the plaintiff's claim but still kept the money and made a profit, then as a cynical wrongdoer, he or she should not be allowed to retain any profit. But if the defendant was innocent, why should the plaintiff gain a windfall because of the skill of the defendant?

A further consequence is the ability to bring an action against third parties. Again, if a third party has knowledge of the plaintiff's claim this may be justified. But there is no good reason for bona fide defendants who obtain the money other than for value to be deprived of that interest in order to satisfy the plaintiff's claim.

Finally, a proprietary interest confers priority on the plaintiff in the event of the defendant's insolvency. Here, the true dispute is between the plaintiff and the other creditors. It may be argued that the plaintiff has a better right to the money because the plaintiff did not choose to take the risk of the defendant's insolvency. Other creditors, by way of contrast, could choose whether to take out a security. But this argument is flawed. Taking a security is often not a practical option, particularly in minor transactions. Moreover, others who did not choose to take the risk of the defendant's insolvency do not gain similar priority, for example, employees and those wronged in tort by the defendant. See further Paciocco, "The Remedial Constructive Trust" (1989) 68 Can Bar Rev 315.

There may be circumstances in which an equitable proprietary interest premised on the defendant's unjust enrichment may be justified, but there are other circumstances in which such an interest is not justifiable. Ultimately, to allow the full consequences of an equitable proprietary interest simply on the basis of an unjust enrichment – that is, on the basis of the factors outlined by Goff and Jones above – is not defensible. A more discriminatory mechanism for finding such an interest must be developed; that mechanism is the remedial constructive trust.

In "Trusts Raised to Reverse Unjust Enrichment" [1996] Restitution LR 3 Birks argues against the adoption of the remedial constructive trust. He claims that it entails judicial discretion, and that Judges should not be expected to make moral judgments between competing claims. He says at 14-15:

> The remedial constructive trust is only needed if the Courts want, and should have a discretion to order defendants to give up things which the law of property says are their own. The legal system ought to think very, very carefully about this .... But there are other possibilities. One might go in the opposite direction, renouncing discretion and sticking to tough legal reasoning. Tough legal reasoning merely means reasoning in the traditional style of the law of property, with the emphasis on legal certainty, against a background in which it is taken for granted that property rights must be closely defined precisely because they hurt third parties.

However, the remedial constructive trust proposed by Lord Brown-Wilkinson is not premised on a broad discretion to simply do what is just. To establish a remedial constructive trust, the defendant must be unjustly enriched, must knowingly retain the plaintiff's property, and no innocent third parties must be affected. The only element of discretion that may arise is in this third element: should the plaintiff have a priority over a third party? Yet even here rules can be developed on the basis of knowledge and solvency, as suggested by Goff and Jones at pp 95-97. And if developed in this way, the remedial constructive trust will result in a great deal more commercial certainty. Not only will the situations in which an equitable proprietary interest arises be certain, but fewer equitable proprietary interests will arise than under the approach proposed by Birks.

CONCLUSION

This case is certainly a victory for traditional equitable doctrines. Equitable proprietary interests arising directly from an unjust enrichment have been rejected, and orthodox trust principles – with the added requirement of knowledge – have been affirmed. The remedial constructive trust does leave some room for equitable proprietary claims in commercial dealings, but these are restricted. First, both unjust enrichment and knowledge must be proved. Secondly, the normal consequences of an equitable proprietary claim will not always apply. This need not lead to judicial discretion and uncertainty if the remedial constructive trust is developed in a principled manner. This approach is to be encouraged. ❑

LITIGATION

edited by
Andrew Beck

CLAIMING EXEMPLARY DAMAGES

This year might well be described as the Year of Exemplary Damages. It has seen the highly significant decisions of *McLaren Transport Ltd v Somerville* [1996] 3 NZLR 424, awarding exemplary damages in a case of negligence, *B v R* unreported, Morris J, 15 February 1996, HC Auckland M1957/93, awarding exemplary damages against a deceased estate, and *G v G* unreported, Cartwright J, 15 October 1996, HC Auckland M535/95, awarding exemplary damages of $85,000 in a case of assault and battery. Despite the highly anomalous theoretical status of exemplary damages, the Courts appear determined to preserve them as a remedy, and quite willing to use them in what they perceive as appropriate cases.

It is well-established that the function of exemplary damages is to punish a defendant for high-handed or outrageous conduct, rather than to compensate the plaintiff for any loss suffered. Although the Courts have acknowledged that the plaintiff gets some satisfaction from the award, it has been stressed that the damages are not related to injury sustained. They are, however, paid to the plaintiff and claimed by the plaintiff by way of a civil proceeding. The formulation of such a claim raises a number of issues.

JURISDICTION

Offences in New Zealand are created by statute, generally with a stipulated penalty; s 9 of the Crimes Act 1961 prohibits conviction of any offence at common law. The jurisdiction to award exemplary damages is, however, apparently a power to punish under the common law. In the past, when damages were largely a matter for the jury, the principles governing awards were ill-defined. The Courts accepted that damages could be inflated so as to have a deterrent role (see eg *Wilkes v Wood* (1764) Lofft 1, 98 ER 489) but as global awards were made, no particular theory of exemplary damages was required.

Now that civil jury trials are rare, Judges have been forced to articulate a reasoned approach to exemplary damages. In England, development has been stunted by the decision of the House of Lords in *Rookes v Barnard* [1964] AC 1129. In New Zealand, the Courts have embraced the concept with a minimum of restrictions. The notion of "civil punishment" has not been seen as troublesome; in *Taylor v Beere* [1982] 1 NZLR 81, the Court of Appeal endorsed punishment as one of the purposes of damages in the law of torts. The jurisdiction to make an award of exemplary damages has not been seriously questioned. It is well established in intentional torts, and has been extended to negligence by *McLaren Transport v Somerville*. It appears, therefore, that the particular category of tort is irrelevant.

Exemplary damages are not limited to torts, however. The Court of Appeal has apparently accepted that they may be awarded for a breach of contract (*Telecom Corporation of NZ Ltd v Business Associates Ltd* unreported, 23 June 1993, CA7/93), and such an award was in fact made in *Tak & Co Inc v AEL Corporation Ltd* (1995) 5 NZBLC 103,887. Awards have also been made for breach of fiduciary duty: see *Cook v Evatt (No 2)* [1992] 1 NZLR 676.

It has never been the purpose of the law of contract or equity to punish those who breach duties: the aim is to provide compensation for loss suffered or disgorging of profits received. By awarding exemplary damages, the Courts have imported a tortious remedy into these areas with only the flimsiest of justification in principle. The message they are apparently sending out is that jurisdiction is not an issue – any breach of duty may give rise to exemplary damages. This conclusion finds some legislative support in s 28 of the Defamation Act 1992, which allows for punitive awards, and s 121 of the Copyright Act 1994 which provides for "additional damages". These were awarded (under the equivalent section of the 1962 Act) in *Criterion Manufacturing Ltd v Eurofurn Industries Ltd* unreported, Greig J, 9 August 1996, HC Auckland CP 207/94.

It is important to note, however, that exemplary damages do not exist in a vacuum – they can only be claimed in respect of an established cause of action: *Tak & Co v AEL Corp*. In *Barlow v Humphrey* [1990] 2 NZLR 373, Fisher J said at 376:

> Exemplary damages do not dangle in the air as a plum to be picked by anyone who happens to pass by. The plaintiff must have an independent cause of action in her own right.

RESTRICTIVE APPROACH

Exemplary damages have always had the potential to get out of control. For this reason, moderation has been urged from the outset. In the leading case of *Donselaar v Donselaar* [1982] 1 NZLR 97 the Court of Appeal expressed the view that immoderate awards would have to be discouraged, and that exemplary damages should not be used to counteract perceived inadequacies in statutory benefits. In *G v S* unreported, Blanchard J, 22 June 1994, HC Auckland CP 576/93, it was said that awards should be limited to "modest amounts". The quantum of recent awards suggests that this is being ignored.

In a recent defamation case, *Television New Zealand Ltd v Quinn* [1996] 3 NZLR 24, the Court of Appeal restated that awards of exemplary damages should be rare. This "principle" has frequently been referred to, but the growing number of claims rather give the lie to it. The survey of recent cases provided by Bruce Corkill in [1996] NZLJ 318 shows that there are many claims in the pipeline, which have clearly been encouraged by the attitude of the Courts.

QUANTUM

The notion that exemplary damages are unrelated to loss suffered by the plaintiff was strongly reaffirmed in *McLaren Transport v Somerville* (at 433). The issue of quantum therefore poses some difficulty.

By definition the defendant's conduct must be outrageous. The scope of the award must then be determined by its degree of outrageousness. Before this year, awards tended to be modest. A total including exemplary damages of $5,000 was awarded for false imprisonment in *Craig v A-G* (1986) 2 CRNZ 551; $7,500 was awarded in *Hayward v O'Keefe* [1993] 1 NZLR 181; in *Shattock v Devlin* [1990] 2 NZLR 88, a case of trespass, $1,500 was awarded against an individual; $5,000 against the police. $4,000 was awarded for unlawfully levying distress in *Metro Mechanical Ltd v Neil Day Motors Ltd* [1995] DCR 232. $5,000 was awarded for breach of fiduciary duty in *SSC & B Lintas NZ Ltd v Murphy* [1986] 2 NZLR 436 and *Cook v Evatt*. A high award of $20,000 was made in *Dellabarca v Northern Storemen and Packers Union* [1989] 2 NZLR 735, although that case involved intentional inducement of breach of contract by a Union. An award of $20,000 was also made in *A v M* [1991] 3 NZLR 228, a case of marital rape; the same amount was awarded in *H v R* [1996] 1 NZLR 299 for sexual abuse over a sustained period. $25,000 was awarded for breach of contract in *Tak v AEL*. That case involved dishonest conduct which the Court considered demanded censure; the award was nevertheless apparently considered modest (see the comments at 103,905).

The position now appears to have altered significantly. In *McLaren Transport v Somerville* a sum of $15,000 was awarded for conduct described as "reckless" and "foolhardy in the extreme". This must be at the lower end of conduct which can be described as "outrageous": see the discussion of the case by Geoff McLay in [1996] NZLJ 318. In *B v R*, $35,000 was awarded, and in *G v G*, damages of $85,000 were awarded. Although the defendant's conduct was undoubtedly reprehensible, the award is well above anything previously contemplated.

Some recent decisions raise the relevance to quantum of factors other than the actual conduct of the defendant. In *McLaren Transport*, Mr Somerville was severely injured, but Tipping J held that he had to guard against being influenced by that factor, the inquiry being confined to the defendant's conduct. In *Tak & Co v AEL Corp*, however, Hammond J considered the importance of international trade to the breedstock industry as a whole in deciding on an appropriate "punishment". In *B v R*, the Court took into account the size of the defendant's estate, and in *G v G*, Cartwright J held that exemplary damages must take into account the extent to which the plaintiff suffers as a result of the defendant's conduct. She also had regard to the means of the defendant, and the fact that permanent name suppression had been refused, in making an award of $85,000.

> ***the injunction to award modest amounts has been cast to the winds. The approach adopted in G v G is akin to a full-scale sentencing***

Because it is the conduct of the plaintiff which is being censured, the defence of contributory negligence does not apply to claims for exemplary damages: *Dellabarca v Northern Storemen and Packers Union* [1989] 2 NZLR 734. Any act of the defendant which has contributed to the plaintiff's conduct would, however, be a relevant factor in determining the quantum of damages.

If the recent trend is to continue, it is clear that the injunction to award modest amounts has been cast to the winds. The approach adopted in *G v G* is akin to a full-scale sentencing, taking into account a large number of factors. This makes it very difficult for a plaintiff to formulate a realistic claim, and could have the effect of prolonging hearings to enable the defendant to introduce evidence on a wide variety of issues.

PLEADING

The Rules of Court do not make any reference to exemplary damages, which traditionally did not have to be pleaded: *Taylor v Beere* [1982] 1 NZLR 1. This arose out of the fact that lump sum awards were made by juries. The modern approach to pleading requires the plaintiff to make the substance of its case known to the defendant, and plaintiffs are required to signal an intention to claim exemplary damages as well as particularising the facts alleged to justify an award: *Witten-Hannah v Davis* [1995] 2 NZLR 141 (CA); *Television New Zealand Ltd v Quinn* [1996] 3 NZLR 24. The amount sought in respect of exemplary damages should also be particularised in so far as the plaintiff is able to do so; the defendant is entitled to know its potential liability in respect of the claim. Suggestions to the contrary in some cases need to be read in the light of the recent Court of Appeal decisions.

ONUS OF PROOF

Because exemplary damages are essentially a punishment claimed in a civil setting, there are obvious issues of onus of proof: is it enough to rely on a balance of probabilities? This has received little attention in New Zealand cases – it is mentioned as a policy consideration in *Tak & Co v AEL Corp* at 103,904, but no consideration was given to the proper standard to be applied on the facts.

The starting point obviously has to be the balance of probabilities, because the proceedings are civil proceedings. Presumably a high degree of proof would be required, by analogy with allegations of fraud. The Courts have, however, not separated exemplary damages issues from other aspects of the case for the purposes of onus of proof. In the end, one is left with the feeling that punishment is being inflicted without the safeguards of the criminal law. Nor are the protections of s 25 of the Bill of Rights available because there is no "offence" with which the defendant is charged.

The issue of double jeopardy where the defendant's act could result in criminal proceedings has not been finally resolved. The Court of Appeal has suggested that this should not be permitted: *S v G* (1995) 8 PRNZ 465, 475. Despite this, a claim following a conviction was allowed to proceed in *O v U* unreported, Heron J, 22 July 1996, HC Hamilton CP 64/95.

PARTIES TO CLAIMS

Where tortfeasors are jointly liable, the general rule is that only a single sum is awarded. This clearly does not cater for exemplary damages, where individual conduct is being punished. It seems that separate awards are acceptable in such cases: *XL Petroleum (NSW) Pty Ltd v Caltex Oil (Aust) Pty* Ltd (1985) 155 CLR 448.

A similar problem arises with vicarious liability: the real question is who ought to be punished. The ordinary purpose of vicarious liability is to provide an effective remedy to the plaintiff; that is not the issue here. It must be established that the conduct deserving censure is essentially that of the employer. Where an agent of a corporation is involved, the corporation will be liable if the act is to be treated as one by the company. An important issue is likely to be whether the representative is liable as well. This will depend on the nature of the act and the particular relationship between the representative and the company: *Trevor Ivory Ltd v Anderson* [1992] 2 NZLR 517 (CA).

A claim for exemplary damages may not be made by an estate; it dies with the victim by virtue of s 3 of the Law Reform Act 1936. It has been held, however, that damages may be awarded against an estate: *B v R* unreported, Morris J, 15 February 1996, HC Auckland M1957/95 (the proceeding was commenced before the death of the wrongdoer). It is not clear how this achieves the purpose of punishing outrageous conduct; deceased persons are not prosecuted for crimes.

SUMMARY

The growth in claims for exemplary damages has no doubt been brought about to a large extent by the decline in the effectiveness of the accident compensation scheme. Generally, however, the Courts have insisted that they are not playing the role of social policy makers, and have confined the role of exemplary damages to one of punishment. While plaintiffs appear to have a reasonable chance of success in such claims, the current situation contains several anomalies, and raises serious questions of both public policy and legal principle.

RECENT CASES

PRECOMMENCEMENT DISCOVERY

In *Hetherington Ltd v Carpenter* unreported, 19 November 1996, CA243/95, the Court of Appeal considered the principles governing precommencement discovery for the first time since its leading decision in *Exchange Commerce Corporation Ltd v New Zealand News Ltd* [1987] 2 NZLR 160, shortly after R 299 of the High Court Rules first came into force. Since that time, two distinct strands of cases have emerged: one adhering narrowly to the wording of the rule and permitting very little by way of precommencement discovery; the other taking a more pragmatic approach, emphasising the benefits of early disclosure.

The case involved actions by shareholders against directors for breach of fiduciary duties and duties of care. The company, incorporated in the Isle of Man, had engaged in a number of transactions which were the subject of challenge, and proceedings had been instituted in the Isle of Man. Although discovery had been provided in the Isle of Man proceedings, those documents were not made available for New Zealand proceedings. The applicants had had difficulty in obtaining information from the company, and therefore sought discovery of company records relating to the transactions in question. The application was refused in the High Court, and the applicant appealed to the Court of Appeal.

Rule 299 requires first that the applicant "is or may be entitled to claim". The Court stressed that there must be "some foundation established such as will make it just that the respondents should be put to the trouble and suffer the intrusion on their affairs which an order will involve". At one end of the spectrum, such discovery will not be granted if the claim, when fully particularised, would nevertheless be struck out. On the other hand, it is not required that a prima facie case be made out. It must be more than a "speculative possibility". This appears to be a slightly wider test than the "real probability of the existence of a claim" as formulated by the Court in the *Exchange Commerce Corp* case; the Court specifically held that the High Court had imposed too high a test.

Secondly, it must be "impossible or impracticable" for the intending plaintiff to formulate the claim without discovery. The Court pointed out that something less than impossibility will suffice, and that the emphasis is on pleading. It also endorsed the view that one of the purposes of the rule is to enable the plaintiff to consider whether proceedings should indeed be issued, and what their scope should be.

In general, the Court of Appeal appears to have endorsed the wider view of the s 299 jurisdiction. In respect of both of the tests, a liberal approach was adopted, and all the major cases endorsing this view, particularly *W v Counties Manukau Health Ltd* [1995] 2 NZLR 560, were referred to with approval. This clearly marks *Hetherington v Carpenter* as the leading case on R 299, which should avoid further argument as to the proper scope of the rule.

On the case before it, the Court was satisfied that there was a sufficient factual basis to the claim to justify preliminary discovery; the fact that the company refused to provide information to the shareholder where the situation required explanation was seen as a relevant factor. The Court held that the Judge was entitled to consider the merits of a proposed derivative action in order to decide whether preliminary discovery was justified, but on this basis too they considered the threshold had been met.

As far as the actual discovery was concerned, the Court stated that the classes of document sought were "generally such as one would expect any public listed company to have in respect of its operations". It was not necessary to go further for the purposes of R 299.

Finally, the Court considered its discretion and said "We see no reason why the Court should exercise its discretion to refuse the application." There were, rather, compelling reasons in favour of discovery. It is of some interest that the discretion was expressed in this way: it suggests that once the jurisdictional requirements have been made out, there is a prima facie entitlement to discovery, subject to the discretion to order otherwise. This interpretation is open to some doubt. Rule 299 is subject to R 312, which requires the Court to make only those orders considered "necessary". In the context, it seems that the Court must exercise its discretion to grant the order rather than to refuse it.

A sobering note is struck by the costs awarded by the Court: a total of $42,500 plus disbursements in respect of the High Court application and appeal. This was in respect of an interlocutory application which the Court considered could have been avoided, and apparently had little purpose. The company had, however, apparently spent some $420,000 resisting discovery. The costs of a whole trial do not bear thinking about.

REMOVAL TO COURT OF APPEAL

Black v NZ Law Practitioners Disciplinary Tribunal unreported, Tipping J, 18 October 1996, HC Wellington CP 224/96 is another chapter in the saga beginning with *Black v Taylor* [1993] 3 NZLR 403. This was (inter alia) an application for removal into the Court of Appeal of an application for review of a decision of the Tribunal.

Tipping J pointed out that the jurisdiction under s 64 of the Judicature Act 1908 is one to be exercised sparingly, and generally not where a prolonged inquiry into facts would be required. Although s 64 does not in terms encompass applications for review, His Honour held that a proper interpretation of the section required them to be included. The fact that this argument was able to be raised suggests that the section – which refers to proceedings made by "notice of motion" – requires some updating.

Most importantly, the substance of the proceeding was found to be a challenge to the Court of Appeal decision in *Black v Taylor*. As there was unlikely to be any prolonged factual inquiry, Tipping J held that it would be entirely futile for the case to be heard in the High Court, which would be bound by the Court of Appeal decision. He held that it was in the public interest, which included the proper use of Court resources, for the matter to be heard in the Court of Appeal, and ordered accordingly.

While cases under s 64 are not common, it is useful to have a clear statement indicating when an application is appropriate. The allocation of Court resources is increasingly a source of concern, and this is clearly an important factor in such decisions.

DISTRICT COURTS ACT 1947 S 59

Section 59 of the District Courts Act 1947 allows the Court to decide matters involving $3,000 or less in accordance with "equity and good conscience". The section has given rise to little case law in recent years, presumably because such matters are resolved in Disputes Tribunals. Three important issues relating to the section were considered by the High Court in the recent case of *Eade v Lockington* unreported, Paterson J, 15 October 1996, HC Auckland HC91/96:

(a) Whether the limit of $3,000 had been exceeded;

(b) Whether any appeal lay from a decision under s 59; and

(c) Whether s 59 could be invoked in a summary judgment application.

Twenty-one lambs belonging to the plaintiffs were allegedly killed by dogs owned by the defendants. Those dogs were in turn destroyed, and the defendants counterclaimed for their value. The total claim was for some $1,500, the counterclaim for $3,000. The District Court Judge, relying on s 59, ordered the defendants to pay the sum of $756 and disallowed the counterclaim.

Monetary limit

The argument was that, in total, the proceedings before the Court involved more than $3,000. Paterson J had little difficulty in determining that this was an incorrect approach: the claim and counterclaim had to be treated separately. This interpretation is clearly correct, and finds support in s 45, which makes specific provision for transfer to the High Court of counterclaims which exceed the jurisdiction of the District Court.

Right of appeal

The Court held that the general principle is that there is no right of appeal from a decision under s 59 unless the case falls within an "established exception". This general principle is said to arise from *Grey v Chapman* (1879) O B & F (SC) 135, a case decided by the Supreme Court based on the Resident Magistrates Act 1867.

The real starting point, however, must be s 71A of the Act, which confers a right of appeal against any order made by the District Court. When *Grey v Chapman* was decided, the right to appeal was confined to points of law; this is expressly referred to at p 137. In addition, *James v Crockett* [1920] GLR 368 makes it clear that an appeal is permitted. In that case an appeal was allowed because a statutory provision had been ignored.

It is suggested that the true position is that the Act does confer a right of appeal, but in most cases – including *Eade v Lockington* – the appeal would be against the exercise of a discretion with which it would be extremely difficult to interfere. To deny the existence of an appeal would mean that an applicant in the Disputes Tribunal would have greater rights, which seems anomalous.

Applicability in summary judgment context

The Court held that a summary judgment application did not constitute a barrier to the application of s 59. It is suggested that this is the correct interpretation. The Court considered that a summary judgment application could be "converted" to a resolution of the case under s 59. It does not seem necessary to go this far. Under the Act, the Court is entitled to "give judgment" pursuant to s 59. There is no reason why such a judgment should not be given on a summary judgment application. The application is simply an expeditious way of bringing a matter to a hearing: the Court has full powers to dispose of the case just as it would at a trial. ❑

TECHNOLOGY TRANSFER TO PACIFIC RIM COUNTRIES

Pierre-André Dubois and Garine Hovsepian of Ogilvy Renault, Montreal

continue their survey by reviewing the countries of the SE Asian Archipelego

PHILIPPINES

LICENSING

Technology transfer agreements in the Philippines are governed by the Revised Rules of Procedure of the Technology Transfer Registry (*TTR Rules*).

The *TTR Rules* require that all technology transfer agreements be approved and registered by the Bureau of Patents, Trademark and Technology Transfer ("BPTTT") for which the Department of Trade and Industry is responsible. In evaluating technology transfer agreements, the BPTTT will consider whether the use of the technology or industrial property rights will favour a substantial contribution to the national development objectives and goals set forth by the Department of Trade and Industry.

The *TTR Rules* provide for the following:

- a royalty rate not exceeding 5 per cent of net sales shall be automatically approved in cases where the agreement involves patent, know-how or trade secret licensing;
- technology transfer agreements must have a fixed term not exceeding ten (10) years with no automatic renewal. In the case of a royalty-free agreement, an indefinite term may be allowed;
- continued access to improvements in the technology shall be made available during the period of the technology transfer agreement;
- the technology supplier shall warrant, to the best of his knowledge, that no third party's intellectual property rights would be infringed by the use of the transferred technology.

The *TTR Rules* prohibit many restrictive clauses in technology agreements, including:

- restricting export territories, except to territories in which the licensor has intellectual property rights on the technology or for which he has granted exclusive rights;
- restricting the use of technology supplied after expiry of the technology transfer agreement, except where early termination is attributable to the licensee;
- grant-back clauses;
- restricting the manufacture of similar or competing products after the expiry of the technology transfer agreement;
- restricting the licensee from obtaining competitive technology, unless the agreement is exclusive;
- tie-in arrangements;
- requiring royalty payments after the agreement has expired or been terminated;
- requiring that the technology recipient shall not contest the validity of any of the licensed patents of the technology supplier;
- restricting the R & D activities of the licensee, even in the field of the technology;
- preventing the technology recipient from adapting the technology to local conditions or introducing innovations, provided that licensor quality standards are not impaired;
- exempting the technology licensor from liability for non-fulfilment of his responsibilities under the agreement or arising from third party claims regarding the licensed product or technology.

The *TTR Rules* also require the technology recipients to submit to the BPTTT annual progress reports and to advise the BPTTT of any modification, amendment, renewal or termination of the agreement.

Provided that the license agreement has been registered with and approved by the Central Bank and the BPTTT, there are no restrictions on the transfer of royalties and fees.

JOINT VENTURES

The entry of foreign investments into the country is regulated by the *Omnibus Investment Code* of 1987 which augments incentive and privileges of investing and is overseen by the Board of Investments, as well as by the Foreign Investment Act of 1991 (Republic Act No 7042) which somewhat relaxed the foreign investment regime. A foreign investor need only register with the Securities and Exchange Commission.

The quality of technology contributions by joint venture partners are set by the *TTR* according to the same criteria for technology transfers involving licensing of intellectual property rights.

Patent laws

The Republic Act No 165, last amended in 1978 by the *Act No 1263*, governs patents. Any assignment must be recorded with the Technology Transfer Registry to be effective against third parties.

MALAYSIA

LICENSING

Under the Industrial Coordination Act of 1975, manufacturing companies with five or more full-time employees and a paid-up capital of RM2.5 million or more are required to obtain a manufacturing license from the Ministry of Trade and Industry ("MTI") for their manufacturing activities. Consequently, all technology transfer agreements involving such companies must obtain prior approval from the MTI. Bank Negara, the national bank, must also approve such agreements.

Guidelines have been issued by the MTI from time to time on required or acceptable terms in agreements. They include:

- requirements that the technology be specifically defined;
- obligation to give the licensee access to improvements known to the licensor, including new patents applied for or registered;
- a royalty rate of 1 per cent to 5 per cent of net sales will be allowed;
- the duration of an agreement should be adequate for full absorption of the technology. While the life of any patent relating to the technology is taken into consideration, an initial period of five (5) years is normally approved and any renewal is subject to prior approval by the MTI;
- a provision for adequate training for the local company's personnel should be included;
- obligations of confidentiality for information covered by the agreement should be confined to the duration of the agreement;
- the agreement should define guarantees with respect to the production capacity, product quality, specifications, and other features of the manufacturing process being licensed;
- there should be no restrictions to sales territory except where the foreign technology supplier is manufacturing directly in another country, where he has given exclusive rights to others or where he is legally not empowered to allow sales based on his technology in an area;
- the agreement must be governed by Malaysian law.

There are no strict restrictions on payments of royalties or transfer of profits, even though permission for payment out must be obtained by the Controller of Foreign Exchange. Permission is usually liberally granted.

Intellectual property license agreements must be registered in order to have legal effect. This does not apply to technical assistance agreements not involving the transfer of intellectual property rights.

JOINT VENTURES

With respect to joint ventures in Malaysia, special regulations covering manufacturing joint ventures exist including guidelines covering equity participation imposed by the Industrial Coordination Act of 1975. Technology transfer agreements through joint ventures are also subject to screening and approval by the MTI.

PATENT LAWS

The *Patent Act of 1983* (No 291), amended in 1993, as well as the Patent Regulations of 1986, amended in 1995, repeal all acts referring to the UK Patent Act, thus providing for a uniform law and procedures covering all three regions of Malaysia (Malaya, Sabah and Sarawak). Transitional provisions exist for patents in force prior to October 1, 1986 and still in force in the United Kingdom.

REFERENCES

Rahman, O A and Kok, T C, "Guidelines for Technology in Malaysia" (1991), in *The Law and Business of Licensing*, Vol 1, 777;

Jayaram, H, "Malaysia: Opportunities, Pitfalls" (1994), in *The Law and Business of Licensing*, Vol 3, 2293;

Industrial Coordination Act of 1975;

Patent Act of 1983 (No 291), as amended in 1993;

Patent Regulations of 1986, as amended in 1995.

SINGAPORE

LICENSING

Singapore has no specific antitrust laws or other types of laws regulating competition or inhibiting transfer of technology. Parties are governed by the law of contract, which is basically the English common law.

Government approval of technology licensing agreements is generally not required. However, if local licensees want income tax exemptions on royalties or fees paid abroad, official authorisation of the agreements by the Economic Development Board is needed.

PATENT LAWS

On February 23, 1995, the Patent Act 1994 and Patent Rules 1995 repealed all acts referring to the UK Patent Act, thus instituting Singapore's own mechanism for original registration of patents. Prior to 1995, UK patents or patents obtained under the European Patent Convention (designating UK as a country) could be re-registered in Singapore. Transitional provisions thus exist for patents granted under the UK Patent Act 1977.

JOINT VENTURES

There are no special regulations in Singapore which control the establishment of joint ventures.

REFERENCES

Jim, T T, "Transferring Technology to Singapore" (1991), in *The Law and Business of Licensing*, Vol 1, 947;

Patent Act 1994;

Patent Rules 1995.

continued on p 458

THE NZ ORDER OF MERIT

G A Macaulay, The University of Otago

finds some quirks in the statutes of our new Order

In January 1995 the Prime Minister established an advisory committee to review the Royal honours system in New Zealand.

The most important recommendation in the committee's report, submitted in September 1995, was that a New Zealand Order of Merit should be instituted to replace the United Kingdom knight bachelorhoods and orders (St Michael and St George, British Empire, etc) but that "dynastic orders" could continue to be awarded.

It is not clear why an advisory committee was needed to recommend discontinuing of British awards. The statutes of none of the orders concerned are part of the law of New Zealand and naturally provide only for the Sovereign of the United Kingdom – a different legal entity from the Sovereign of New Zealand – to make appointments to them.

It is also not clear how the "dynastic orders" (the Order of the Garter, the Royal Victorian Order, and the Order of Merit) can be part of the New Zealand Royal honours system. They are not orders of a dynasty or of some supranational monarch, but are orders of the Sovereign of the United Kingdom only, awarded without ministerial advice. The Queen, as Queen of New Zealand, cannot make appointments to the Order of the Garter: it would be a legal and constitutional absurdity.

On 30 May 1996 the Queen issued a Royal Warrant (SR1996/205) creating the New Zealand Order of Merit, and the first appointments to the order were announced in the Queen's Birthday Honours shortly afterwards.

The statutes are in most respects in accord with the recommendations of the advisory committee and establish a five-class order (the classes are democratically called "levels") with ordinary members (New Zealanders and citizens of the Queen's other realms), additional members (appointments above the normal quotas for each class), and honorary members (citizens of Commonwealth countries of which the Queen is not head of state, and foreigners). The Queen is Sovereign of the Order; the Governor-General is Chancellor; and there are two other officials (confusingly called "officers" – the name for members of the fourth level – in a marginal title), a Secretary and Registrar and a Herald. The statutes also specify the insignia (which include lapel badges for everyday wear but which otherwise follow the pattern of the Royal Victorian Order; the sash and ribbons are "ochre", a deep red) and deal with procedural matters and armorial privileges.

The specific recommendation of the committee that the titles "Sir" and "Dame" not be used for any future honours was not adopted and the statutes provide for those titles to be used by members of the first and second levels.

Provision is made for the cancellation of appointments to the order in appropriate cases, but there is still no codified provision in New Zealand law for depriving a knight who has received the accolade of the title "Sir".

A novelty is the use of the terms Knight and Dame Grand Companion and Knight and Dame Companion for members of the two highest classes. The one-class Orders of the Garter and Thistle have Knights and Ladies Companions, but the other current United Kingdom orders of knighthood use the terms Knight and Dame Grand Cross and Knight and Dame Commander. In the Orders of the Indian Empire and the Star of India the term Knight Grand Cross was replaced with Knight Grand Commander to avoid giving offence on religious grounds and it would be interesting to know why this precedent was not followed.

It would also be interesting to know why the opportunity was not taken to absorb the Queen's Service Order into the new order; instead, the advisory committee has recommended that it be reconstituted as a one-class order solely for the recognition of voluntary community service. New Zealand has a small population and a special order for just one category of meritorious service is difficult to justify in the context of reforms which otherwise simplify the honours system and which do not even include a military division in the new order. The very name of the Queen's Service Order is a problem: what will it be called when the Queen is succeeded by a king, or if New Zealand becomes a republic?

The statutes of the New Zealand Order of Merit include a number of curiosities. Statute 25 ordains that from the Collar of the Order (in effect a chain of office for the Sovereign and her representative) shall hang something called the badge of the Order, but that is nowhere defined. Presumably what is meant is the badge of the first level of the Order; the badges of the other levels differ in size and materials.

Statute 35 ordains that the Sovereign and Knights and Dames Grand Companions shall wear a sash from which shall hang their badge. This is a rather anachronistic provision: white tie functions are virtually extinct in New Zealand – even State Dinners are black tie occasions – so it is not clear when a Knight Grand Companion would wear his sash. It is not even clear when the Queen or Governor-General would wear the sash as they are to wear the collar of the Order at investitures and presumably at State Openings of Parliament, and Statute 26 specifically forbids the sash and collar being worn together.

Statute 16 authorises the Governor-General to confer the accolade of knighthood on Knights Grand Companions and Knights Companions who have not previously been knighted. Statute 20 authorises ordinary and additional members of the first and second levels of the order to be called "Sir" or "Dame". It is not specified, however, that men in the first two levels must be knighted, and so the possibility has been created for a man to be called "Sir" without receiving the accolade. Is knighthood to be optional for Knights?

In particular, it is not clear if Knights Grand Companions and Knights Companions who are citizens of the UK, Canada, Australia, or other countries of which the Queen is Sovereign are to receive the accolade from the Sovereign of New Zealand (or her representative) or to call themselves "Sir". It should be borne in mind that neither the Sovereign of Canada nor the Sovereign of Australia, on the advice of her ministers in those realms, confers the accolade of knighthood or titular distinctions upon her subjects.

This confusion would have been avoided if those drafting the statutes had recognised the reality that the various Crowns in the Commonwealth have for many years been separate and that there is no legal tie, only a personal link, between the Crowns of New Zealand and Australia and the United Kingdom and so on, and that it is inappropriate for the Sovereign of New Zealand to legislate for or to give favoured treatment to the subjects of those other Crowns.

It would have been more appropriate either for ordinary and additional membership of the Order to be restricted to New Zealanders, and honorary membership extended to comprehend all non-New Zealand appointees (including Britons, Australians, etc) or for there to be no honorary membership at all but a statute included specifying that non-New Zealanders would not receive the accolade or be entitled to be called "Sir" or "Dame" (in the same way that British clergymen who are appointed KCVO, for instance, do not receive the accolade, or call themselves "Sir", or transmit the title "Lady" to their wives).

THE HERALDIC PROVISIONS

Statute 50 permits members of the Order to embellish their arms with their collar, the circlet of the Order, and their badge, as appropriate, and for Knights and Dames Grand Companions to be granted supporters.

It is of course entirely appropriate for the Chancellor to encircle his or her arms with the collar of the Order, but curiously this privilege is extended to former Chancellors as well. An office-holder who impales the arms of his office with his personal arms ceases to do so upon relinquishing office; a king who abdicates ceases to use the Royal crown above his shield; a disclaiming peer does not use the exterior additaments of his peerage (coronet, peer's helmet, and supporters) with his arms; so it is strange that a retired Governor-General should continue to be identified armorially as Chancellor of the Order.

The most curious aspect of the armorial privileges, however, is that they are restricted to those members of the Order whose arms have been granted or confirmed by Garter Principal King of Arms (Statute 50): armigerous Scots, Canadians, or South Africans who are appointed to the Order are evidently to be denied the privilege of adding their insignia to their achievements unless they pay to have their arms recorded at the English College of Arms, and members of the Royal Family whose arms are assigned by Royal Warrant (and neither granted nor confirmed by Garter) are similarly disadvantaged.

Why Garter should be mentioned in the statutes at all is baffling, as his office is otherwise unknown to the law of New Zealand; he is appointed and paid by the Sovereign of the United Kingdom and has no authority in or over New Zealand or New Zealanders. Conversely, the Sovereign of New Zealand has no authority over Garter (or any other servant of the Crown of the United Kingdom) so the provision of Statute 50 that Knights and Dames Grand Companions may be granted supporters by Garter is an empty privilege: Garter cannot take official notice of a Royal Warrant of a Sovereign other than his own.

Provision is made by Statute 51 for a Herald of the Order. This is the first genuinely New Zealand heraldic office – New Zealand Herald of Arms is, despite his title, a herald of England (as is demonstrated by the fact that he wears English regalia and insignia and acts as deputy in New Zealand of Garter, a role which may be taken only by a herald of England) – and so it is a pity that no provision is made for his insignia to be added to his heraldic achievement (the Secretary and Registrar is similarly neglected).

It is indeed unfortunate that the Statutes of the New Zealand Order of Merit have been so poorly drafted, perhaps because they were prepared too hastily and without adequate consultation, and it is ironic that an enactment designed to patriate much of New Zealand's honours system should have such anglocentric and anachronistic heraldic provisions embedded in it. ❑

continued from p 456

INDONESIA

There is no substantial legislation on the review of license and technology transfer of technical assistant agreements in Indonesia. In general, license agreements do not require initial government approval. However, the parties must submit periodic reports to the Indonesian Government Coordinating Board (Badan Koordinasi Penanaman Modal or BKPM) as well as to the Bank Indonesia and the government department responsible for the relevant industry. Restrictions exist on maximum royalty rates in certain industries, including in the textile and pharmaceutical industries.

A license agreement should not contain any provision which could be considered as harmful to the Indonesian economy or restrict the ability of Indonesians to master the technology.

Indonesia has no foreign exchange controls.

JOINT VENTURES

All foreign investments, including joint ventures, must ultimately be approved by the President of Indonesia, administered by the BKPM, according to Government Regulation No 20 of 1994 by which foreign investment regulations were significantly relaxed.

PATENT LAWS

Patents are regulated by *Law No 6/1989*, which became effective on August 1, 1991. Prior to the *Law No 6/1989*, applications were simply held in abeyance pursuant to the Government Announcement of August 28, 1953. Special transitional rules were enacted to deal with foreign applications under the International Convention (Paris) to allow for patent protection if filed in Indonesia by July 31, 1992. Patent licenses must be registered at the Patent Office.

REFERENCES

Government Regulation No 20 of 1994;

Law No 6/1989;

Government Announcement of August 28, 1953. ❑

PREDDY – ISSUES FOR NEW ZEALAND'S LAW OF THEFT AND FRAUD

Frank Quin, an Auckland lawyer

discusses the recent controversial decision of the House of Lords in* R v Preddy *[1996] 3 WLR 255 and aks what would have been the outcome in New Zealand?

THE DECISION IN *PREDDY*

In *Preddy*, the House of Lords overturned the decisions of the Court of Appeal upholding convictions under s 15 of the Theft Act 1968 on counts of obtaining property belonging to another by deception. The property in question was alleged to be the choses in action generated by electronic funds transfers from bank accounts maintained by certain building societies to bank accounts maintained by the appellants or their solicitors. The deception lay in falsehoods contained in mortgage loan applications submitted by the appellants to the building societies which induced them to arrange for the electronic transfers.

The Court of Appeal had found that these transfers amounted to "intangible property" and therefore "property" for the purposes of s 15. In the House of Lords, the main judgment was delivered by Lord Goff of Chieveley. He doubted, but did not decide, the correctness of this proposition. The crucial question, and one seemingly overlooked by the Court of Appeal, was whether such "property" as had been obtained was property "belonging to another", as required by the section.

In this regard, the Court of Appeal's decision could not be allowed to stand. Even if it was permissible to treat as "property" the credit entries in the bank accounts of the appellants or their solicitors by virtue of the electronic transfers, manifestly these were *the appellants'* property. In the words of Lord Goff (at p 264):

> ... when the bank account of the defendant (or his solicitor) is credited, he does not obtain the lending institution's chose in action. On the contrary, that chose in action is extinguished or reduced pro tanto, and a chose in action is brought into existence representing a debt in an equivalent sum owed by a different bank to the defendant or his solicitor.

THE IMPLICATIONS FOR ENGLISH LAW

The result appears to be that, under English law, there is no criminal liability for duping a finance company into advancing a loan. This seems extraordinary when regard is had to the wholesale, and radical, reform which the Theft Act 1968 represents. Moreover, it is not just the fact that the funds transfers were electronic in nature which exposed this inadequacy. In some instances, the loan moneys were advanced by cheque. Although the case stated to the House of Lords concerned only the electronic transfers, Lord Goff went on to hold that s 15 of the Theft Act was not available with the cheque cases either.

In a commentary on the "legislative history", Lord Goff noted that the offence of obtaining credit by fraud as included in the Bill, which *prima facie* would have covered the appellants' conduct, had been withdrawn before enactment. It was replaced by a provision which caused much difficulty thereafter and which was eventually jettisoned and replaced by a new crime of obtaining services by deception, in s 1 of the Theft Act 1978. There is however a Court of Appeal decision (*R v Halai* [1983] Crim. L. R. 624) to the effect that this offence does not lie in the case of so-called "mortgage frauds". Whilst doubting this decision, it was not open to the House of Lords in *Preddy* to overrule it. Lord Goff contented himself with noting that the Law Commission has "prepared a simple two clause Bill" which, if enacted, would bring such activity within s 1 of the 1978 Act. It may be noted in passing that this is the sort of piecemeal tinkering which had plagued the English law of theft and fraud for centuries and which the Theft Act 1968 was supposed to obviate.

Such is the unsatisfactory state of affairs in England. Incidentally, the judgment in *Preddy* notes that, had the appellants operated their scheme in Scotland, they would have been ensnared by the crime of fraud at common law which, apparently, consists of "bringing about some definite practical result by means of false pretences"! But how would they have fared in New Zealand?

NEW ZEALAND'S LAW OF THEFT AND FRAUD

Our Crimes Act 1961 is a direct descendant of the *Draft Code of Criminal Law* prepared by the English jurist Sir James Stephen in 1878. It had occurred to Stephen that such a code could usefully be produced from his *Digest of the Criminal Law*, published the previous year. While his work on the code was recognised by the appointment of Royal Commissioners (of which he was one), to Stephen's chagrin the *Draft Code* never became law in England itself. It was however adopted in New Zealand, as the Criminal Code Act 1893, and in certain other colonies (notably Canada, South Africa and some Australian states).

The 1893 code was re-enacted with some refinements as the Crimes Act 1908 which in turn became the current Act of 1961. As regards the content of Part X of the 1961 Act, headed *Crimes Against Rights of Property*, as enacted this differed little from the 1893 legislation. There have been subsequent additions, one of which is of direct relevance and will be noted below.

In the second edition of his seminal *Criminal Law and Practice in New Zealand*, Sir Francis Adams described (at para 1686) the *Draft Code's* treatment of theft and fraud as "without doubt, a masterly simplification and amelioration of the law". Foremost in his reasons for this accolade was the drafting of the crime of theft (s 220 of the current Act) which, in its extension to *conversion* as well as asportation, unshackled our law from the common law's conception that theft reposed in a *taking* of a thing out of another's possession. This notion had given rise to myriad difficulties, and resultant qualifications, in English law.

A further improvement was introduced in relation to the crime of obtaining by false pretences. Under English law at the end of the 19th century (and indeed until the Theft Act 1968), this crime was committed only when *legal ownership* of a thing was transferred by means of a deception. Where the deception was found to have produced a transfer only of physical possession, liability had to be founded, if at all, on the common law crime of larceny by a trick. This distinction, the source of so much confusion in English law, was removed by the drafting of what is now s 246 of the Crimes Act 1961.

A more controversial reform was the creation of a new crime, now s 222 of the current Act, in place of the English crime of "fraudulent conversion". Sir Francis Adams (*ibid*, at para 1791) described s 222 as "perhaps the most difficult section of the Act". In this writer's view, it is certainly the least understood of all the provisions in Part X of the Act. What is thought to have been Sir James Stephen's intention in drafting this offence (for s 222 is *verbatim* the equivalent provision in the *Draft Code*) was the creation of a crime of theft of beneficial proprietary interests recognisable *only in equity* and, for that reason, not protected by a criminal law based on the common law's perception of ownership reposing in possession of a thing *in specie*. But, regrettably, the jurisprudence to date on s 222 has become fudged by recourse to the English law notion of a "fiduciary obligation" as the basis for liability and has thus produced the same difficulties as to when liability arises as was the case with fraudulent conversion under English law.

APPLICATION TO ELECTRONIC FUNDS TRANSFER

Whilst it is possible to point to these ways in which, with the adoption of the *Draft Code of Criminal Law*, New Zealand's law of theft and fraud freed itself from the vagaries of English law, it does not follow that it would have addressed the conduct at issue in the *Preddy* case.

The principal reason is that both "common" theft under s 220 and obtaining by false pretences under s 246(2) apply only to "anything capable of being stolen". This expression is defined in s 217 as embracing every "inanimate thing" which "either is or may be made moveable". In other words, for a thing to be amenable to theft it must be *tangible* (the one exception being electricity – see s 218).

In this respect, New Zealand law has yet to embrace the reform under the English Theft Act 1968 which, as noted in outlining *Preddy*, defines "property" to include intangibles.

So it can be said that the appropriation of a chose in action, such as copyright in a work, cannot be the subject of theft or obtaining by false pretences. By the same token, no such liability will lie for the downloading of data from a computer, or from the Internet by means of a computer.

Pausing to consider the cheque cases in *Preddy*, these would on the face of it have fallen squarely within subs (1) of s 246. By means of the false pretence represented by the mortgage application form, the building society would have been induced to "execute" a "valuable security", defined (in s 2(1)) to include a cheque. Because there is no requirement that the valuable security be the property of another person, the difficulty for the prosecution identified by Lord Goff in *Preddy* would not be encountered.

But it is fairly clear that this limb of s 246 would not be available in respect of the electronic funds transfer cases. Although not spelt out, it is unlikely that the definition of "valuable security" can be extended to an *intangible* representation of a chose in action, such as an electronic impulse within a bank computer system.

In point of fact, New Zealand's law of theft and fraud has yet to include any provisions aimed specifically at electronic technology. Given the now pervasive use of computers and electronic communications in modern society, this is an area well overdue for attention by the Legislature. Electronic payment systems are no longer confined to "wholesale" inter-bank transfers. EFTPOS (electronic funds transfer at point of sale) is becoming the preferred payment method in many retail sectors and we are now seeing the emergence of a range of "smart card" or "stored value card" payment systems (such as Mondex). As the Internet grows in public acceptance and usage, there will be increasing recourse to "on-line" computer-resident payment mechanisms (such as the "ecash" electronic coin being developed by Digicash of The Netherlands).

AVAILABLE CRIMES – CREDIT BY FRAUD

Returning to the facts in *Preddy*, which after all could just as easily have occurred in New Zealand, there would appear to be two crimes available to the prosecution here. The first is obtaining credit by fraud under s 247 of the Crimes Act. This is the offence which, Lord Goff noted with apparent bemusement in *Preddy*, has except in very limited circumstances been expunged from English law.

Undoubtedly, the word "credit" in s 247 is flexible enough to embrace the bank credit in favour of the appellants in *Preddy* which was generated by the electronic funds transfer. Section 247 has its origins in the English offence created by the Debtors Act of 1869 which, following the common law, was a misdemeanour rather than a felony. This explains why the section carries a penalty of only one year's imprisonment compared with the seven years for obtaining by false pretences.

AVAILABLE CRIMES – FRAUDULENT USE OF A DOCUMENT

But the crime which is much more likely to be resorted to, on the facts in *Preddy*, is that created by s 229A of the Crimes Act, inserted into the Act by the amendment of 1973. The writer has commented on s 229A at length at [1996] NZLJ 330.

Section 229A is entitled "Taking or dealing with certain documents with intent to defraud". Originally conceived (by the Criminal Law Reform Committee) to address the theft and fraudulent use of documents such as airline tickets and credit cards, in practice the section is being invoked – successfully – in all manner of fraud cases where there is some use of a document which can be said to be "capable of being used to obtain any ... pecuniary advantage".

In particular, the section has become the crime of choice with so-called benefit fraud where the document having this requisite capability is typically a benefit application form. The analogy with the mortgage loan application form in *Preddy* will be obvious. In any event, there have been at least two cases under s 229A which involved hire purchase financing applications. What emerges clearly from a review of cases on the section is that establishing a document's capability to generate pecuniary advantage has been the least of the prosecutor's concerns and that, in the vast majority of cases, the substantive issue has concerned the defendant's state of mind.

as a matter of policy specific offences should be identified, so that citizens could know with some degree of certainty the boundaries of lawful conduct

THE POLICY ISSUE

In his remarks on the background to the Theft Act 1968, Lord Goff of Chieveley observed that as enacted it represented the primacy of one of two opposing schools of thought on fraud offences. That which was defeated has it that, in the words of Lord Goff, "there should simply be a general offence of fraud, the essence of which is (broadly speaking) dishonestly deceiving another for the purpose of gain". The view which prevailed was that this approach was undesirable and that as a matter of policy specific offences should be identified, so that citizens could know with some degree of certainty the boundaries of lawful conduct and so that conduct of a minor or regulatory nature, already covered by specific statutes, would not be swept up by an all-embracing crime of fraud.

Lord Goff, supported in this regard in the brief judgment of Lord Jauncey of Tullichettle, noted that the broad common law crime of fraud in Scots law "appears to suffer from no adverse consequences in practice, no doubt because of the good sense of the prosecuting authorities".

As the writer noted in his commentary on s 229A (see above), in its wording and application in recent years this section is offering prosecutors the flexibility which would be expected of a general crime of fraud. Yet ironically the section was conceived with quite specific evils in mind. It is the fact that most conduct of any complexity, and particularly of an economic nature, involves the use of some document, coupled with the growing tendency to equate "intent to defraud" with "dishonestly", which is making s 229A the proxy of all the mainstream crimes against rights of property.

LIABILITY FOR DISHONEST THOUGHTS?

In his earlier commentary, the writer's central thesis was that by s 229A the law of New Zealand is coming close to imposing criminal liability for dishonest thoughts. Since publication of that commentary, the Court of Appeal has delivered judgment in *Ruka v Department of Social Welfare* (1 October 1996). The majority decision, to overturn convictions under s 229A for "benefit fraud", has gained media attention because of the focus on the "battered woman syndrome". None of the five Judges was moved to comment on the issue whether the section is properly used in such cases given the specific offence under the Social Security Act.

But buried in the lengthy judgments is brief mention of an argument which the Crown attempted to run in the Court of Appeal. As recorded in the combined judgment of Richardson P and Blanchard J, counsel for the Crown submitted that, whether or not the appellant had been living in a relationship in the nature of marriage, liability arose under s 229A:

> ... because, as has been properly conceded by her counsel, [appellant] did set out to obtain a benefit to which, *incorrectly*, she believed herself not entitled; therefore, she attempted *with intent to defraud* to use a document for pecuniary advantage.
>
> (Emphasis added.)

This submission was rejected not on its merits but because it was too late in the piece for the Crown to take the point. If accurately recorded, the prosecutor's submission was that liability under s 229A arises for doing something which is permissible in law where the actor has a mistaken belief that the act is *not* permissible. In other words, that the section imposes liability for dishonest thoughts and nothing more. The submission ought to have been rejected as being, to borrow the words of Lord Ellenborough CJ in the early 19th century, "mischievous in principle and supported by no authorities in law". It is a measure of s 229A's acceptance into mainstream criminal law that this proposition, fundamentally at odds with our notions of criminal justice, was rejected purely on procedural grounds.

CONCLUSION – THE LESSON FROM *PREDDY*

As noted earlier, the facts in *R v Preddy and Others* could easily occur in New Zealand. Increasingly, businesses are using electronic funds transfers to effect and receive payments. Because of the intangible nature of the proprietary interests at play, our traditional law of theft and fraud will be found wanting. Recourse will be had to s 229A, if there is a physical document used as part of the conduct. Unsatisfactory decisions are likely to follow as the section is again applied in ways never envisaged by its promoters. Of course, if there is no physical document having the requisite capability under the section, it will not be available. The offence of obtaining credit by fraud may prove to be the only criminal provision available. If a large amount of money is involved, this offence – commonly associated with decamping from a restaurant or a taxi without payment – will find itself in a spotlight for which it was never intended.

The moral is plain to see. Reform of our law of theft and fraud should be back on the legislative agenda and, this time, with a resolve to see it through. ❑

LAWYERS' ATTITUDES TO COMPETITION AND ADVERTISING

Michael Fay and John Bell of the Department of Marketing, University of Otago

surveyed lawyers and other professional groups in 1985, in 1988 and in 1994 to discover their attitudes to competition and advertising within the profession. This paper explains how attitudes have changed over that period

INTRODUCTION

The historical role of New Zealand as an exporter of agricultural goods to the United Kingdom, had produced a highly regulated and subsidised internal economy. Outside of the agricultural sector, where New Zealand was extremely internationally competitive, the country's economy was protected and uncompetitive. The move by the United Kingdom towards Europe and membership of the EEC, led to a diminishing of the special relationship between the United Kingdom and New Zealand. This change produced pressure on the value of New Zealand's economic base, exacerbating instability within the economy. New Zealand governments were slow to accept the new realities, and it was not until 1984 when the time for measured adjustment was long passed, that a change of government signalled a profound change in the way that the country would organise its economic affairs. In a few years the economy changed from being among the most protected of western economies to being among the most open to domestic and international competition. The professions were not immune from this new economic spirit. To a varying extent they all began a process of moving away from official and institutionalised collegiality, and towards behaviour that fitted more closely with the economic philosophy of Friedmanism.

In the kind of dynamic economic and social environment that existed in New Zealand in the 1980s, the relationship between a profession's code of practice and the behaviour and aspirations of the members will tend to be unstable. Typically there will be a loose or unorganised grouping of often younger members who wish to break free from a set of constraints that they believe to be no longer relevant to their working experience. The professional hierarchy, often comprised of older members, eventually responds to this pressure, but in so doing goes further than the more conservative members of the profession are happy to accept (Hite and Fraser "Meta-analysis of Attitudes Towards Advertising by Professionals" (1988) 52 *J of Marketing* 95., Siebert W. S. "Advertising and the Professions" (1984) 84 *Intnl J of Advertising* 189). The present code of practice for advertising by legal practitioners in New Zealand allows considerable latitude, which can be illustrated with some current examples:

- Half pages in Yellow Pages detailing the appeals of a particular practice: eg all female staff, specialist services, and carrying photographs of the partners.
- The quick fix "DIAL-A-LAWYER 24 HRS" (at $4-95 per minute).
- Flights of whimsy, eg "Let Me **Mastermind** All Your Legal Needs" (from the winner of an intellectual TV quiz show).
- Small advertisements placed among those for escort services and confidential pregnancy advice, often using colloquial language, eg "Busted?"
- Full colour pages in national magazines using all the creative crafts of advertising agencies.

It was suspected that the changes in attitudes and behaviour under way within the profession were indicative of what might become a fundamental shift in the place and role of the professions in society. Consequently it was concluded that these changes should be monitored. Members of the legal profession, and also of the medical, dental, veterinary, and accounting professions, were surveyed in 1985 (Fay and Bell "Competition, Advertising, and the Professions: A Cross-Professional Comparison" (1989) 11 *N Z J of Business* 33), and subsequently in 1988 (Bell and Fay "From the 'Gentleman' to the 'Marketer': The Changing Attitudes of the Professions in New Zealand" (1991) 10 *Intnl J of Advertising*, 205) and in 1994. This paper presents the findings of the combined surveys, detailing the changes in attitudes that occurred over the nine year period.

DATA COLLECTION

A current membership list of the New Zealand Law Society was edited to eliminate those members clearly not in private practice. Systematic random samples (1985, n = 300; 1988, n = 300; 1994, n = 500) were drawn, and selected individuals mailed a self-completion questionnaire, a covering letter from the Dean of Commerce at the University, and a reply-paid envelope. No follow-up mailing was used. The questionnaire contained:

(i) Forty 5-point Likert scales with response categories ranging from strongly agree to strongly disagree.
(ii) Ten questions on the advertising of specific elements of the practice.
(iii) A request for demographic data.

Response rates (usable responses as a percentage of total mail-out) were: 1985 = 64 per cent; 1988 = 36 per cent; 1994 = 48 per cent. There was no evidence that the variation in response rates between the survey years was related to systematic bias (age, location, gender) that might have invalidated cross year comparisons.

RESULTS

For each attitude statement, weights of 1 (strongly agree) to 5 (strongly disagree) were assigned to the response categories. One way analyses of variance and Tukey tests were carried out to compare the mean ratings for each scale across years. Attitude statements have been grouped under the following headings:

(i) Competition.
(ii) Fees.
(iii) Client Relationships.
(iv) Advertising.

An asterisk against the 1985 figure indicates a significant difference between the ratings for 1985 and 1988 at p0.05, an asterisk against 1988 shows that the difference between 1988 and 1994 is similarly statistically significant, and against 1994 that the comparison of 1994 and 1985 is significantly different.

To evaluate changes in levels of support for the advertising of specific characteristics of a professional practice over the three studies (Table 2), Chi Squared tests were carried out. Unless indicated by a superscript ^{ns} against the derived Chi Square figure, the change is statistically significant at p 0.05.

COMPETITION AND FEES

With the exception of fee competition, the direction of the changes in mean ratings of all the "competition" statements were towards greater acceptance of a competitive environment. This move towards acceptance of a competitive professional environment is reflected in all of the professions that were surveyed.

Table 1
Mean ratings for "Competition" statements

	1985	1988	1994	F
The members of my profession are colleagues, not competitors	3.02	2.85*	3.15	3.34
Competition between members of my profession in the level of fees they charge is *un*desirable	3.39*	3.00	52.87*	11.50
Competition between members of my profession through advertising is *un*desirable	2.94	3.05	3.17	2.23
I look forward to the day when members of my profession can compete openly	2.96	3.05*	2.48*	19.96

Concern over the effects of fee competition is not unusual among the professions, but a drift away from a positive attitude towards fee competition is unusual. This may be because, in 1985 when the first survey was carried out, the legal profession exhibited quite enthusiastic attitudes toward a then largely unexplored competitive environment. Since then there has been time to learn of the problems of "fee" or "price" competition; price reduction is easily copied by competitors and can lead to the product or service being treated as an undifferentiated commodity (Bollard and Scott "Competition and the legal profession" [1996] NZLJ 275). This can, in turn, lead to shopping around and frequent switching between legal advisers.

Although the legal profession is seen by many, both inside and outside of it, as having adopted a highly commercial orientation, this view is not supported by reaction to the "Fee" statements. Apart from a small increase in the numbers prepared to negotiate the fee, there was no statistically significant change in attitudes towards client charging. Particularly interesting is the continuing high level of agreement with the statement that "Professionals should be prepared to reduce their fees for clients with limited ability to pay", which is not compatible with a profession dominated by money.

Table 2
Mean ratings for "Fee" statements

	1985	1988	1994	F
Professionals should be prepared to reduce their fees for clients with limited ability to pay	2.15	2.13	2.21	0.38
It is quite reasonable for professionals to raise their fees for clients who are clearly able to pay	2.92	2.81	2.97	0.80
I am prepared to negotiate the fee with a client	2.11	2.08	1.96*	3.31
I try to get my patients to pay before they leave the building	3.64	3.56	3.50	1.06

CLIENT RELATIONSHIPS

It is clear that there is a belief in the profession that relationships between lawyer and client are changing, with small but consistent movement in reaction to each attitude statements. Clients are seen as more demanding, to be ready to change their legal adviser, and consequently be less inclined to have a long term relationship with the provider. If these perceptions are accurate, the profession might ponder the extent to which these changes are an inevitable consequence of a more competitive and profit oriented culture, or are a direct consequence of the business behaviour of legal practices. Legal practices have a difficult problem compared with other professions in that they offer a wide range of services that have very little relation to each other, and for the individual client may be carried out at all over a long time period. Thus an effective "new client" strategy for the legal practice is to advertise the particular transaction (conveyancing, marijuana possession defence, marriage breakdown), but to retain the client this particular interaction must then be converted to one of being a generalised "legal adviser".

Table 3
Mean ratings for "Client relationships" s tatements

	1985	1988	1994	F
I expect my professional relationship with a client to be a long-lasting one	1.82*	2.05	2.04	4.93
Clients are more demanding today than they used to be	2.12	2.07	1.90*	3.83
Clients are more likely to change from one professional consultant to another than they were a few years ago	2.05	1.91	1.79*	7.06

Broadly speaking, it is more expensive to gain new customers than retain existing ones, particularly in markets where supply is easily able to meet demand. This situation is reflected in academic and commercial marketing thinking that is stressing continuing association between provider and supplier, under the rubric "relationship marketing".

ADVERTISING

Of the sixteen attitude statements concerned with advertising, only five showed any significant change over the nine year survey period. All of these changes were in the direction of a more accepting and relaxed attitude towards advertising, including a diminishing belief that advertising will increase the level of profits. Our judgment is that after a decade of experience with advertising, legal practitioners have realised that it is far from being all-powerful. Both its strengths and limitations are now known, and are comfortably lived with.

In view of the nature of the some legal advertising, that would be difficult to argue as not containing a persuasive component, it is of interest to note the small move in attitude for the data on "persuasive advertising" (from 3.66 in 1985 to 3.44 in 1994; 3.00 = Neither agree nor disagree).

Table 4
Mean rating for "Advertising" statements

	1985	1988	1994	F
Competition between members of my profession through advertising is *un*desirable	1.92	2.19	2.40*	11.39
Advertising would result in higher fees	3.06	3.21	3.45*	8.33
Advertising would allow me to expand my business	3.02	3.02	2.77*	4.33
If members of my profession are allowed to advertise I will make more money	3.40*	3.64	3.84*	15.69
The least competent members of my profession have the most to worry about if the rules on advertising are relaxed	3.20	3.38	3.55*	6.81
I would not oppose any moves allowing members of my profession to place persuasive advertising	3.66	3.57	3.4	42.59

When asked about attitudes towards specific types of informative advertising, the division of feelings between the provision of general information, and information directly related to money, was again evident. Support of advertising to inform prospective clients of fees levels and of the existence credit facilities showed no movement between 1988 and 1994.

Table 5
Percentage of respondents in favour of specific types of advertising information

	1985	1988	1994	X^2
Office hours	94	99	95	4.49^{ns}
Location	95	99	96	2.92^{ns}
Fees	34	50	47	9.97
Years in practice	44	63	73	39.10
Services offered	91	96	97	2.62^{ns}
New staff	44	66	73	39.16
Age	30	49	53	23.53
Specialism	77	82	82	2.19^{ns}
Awards	22	33	51	40.33
Credit facilities	40	45	42	0.80^{ns}

DISCUSSION

Of the five professions that we have surveyed since 1985, the legal profession has always been among those with a more positive attitude towards a commercial orientation in general, and towards advertising in particular. However, in the early days of the move towards an openly competitive professional structure there was widespread concern over where the new orientation might take the profession. These concerns appeared to have two roots: a dislike, even disdain for the crasser aspects of commercialism, and an exaggerated view of the power of advertising to change the nature of the provider/client relationship. However, after a decade of experience of advertising, its power and effects have been put into perspective. The move from a controlled and protected economy to one exposed to the full and sometimes icy blast of international competition, the speculative property and share market boom and bust of the late eighties with consequent claims on the lawyers' fidelity fund, the falls and rises of a free floating currency, and the continued selling of state assets, have been events of greater substance. Alongside the other changes that have occurred in the New Zealand commercial sector, the effects of advertising have to be judged as relatively minor (O'Donohoe et al. "Marketing Principles and Practice in the Accounting Profession: A Review" (1991) 25 *Eur J of Marketing* 37). Open competition and advertising are now part of the daily experience of practising lawyers, with advertising just one of the business building or sustaining tools available to the practice.

It seems likely that the change in attitudes observed in the legal profession, and in the other professions studied, are a reflection of a widespread shift in attitudes and values in New Zealand society. Farming is less about "life-style" and more about "return on investment", a house has become less of a lifetime home and more of a "property" to be bought and sold as part of an individual's wealth creation policy, and Commerce has encroached on Arts as the "normal" tertiary education. It would be surprising for the professions to have stayed aloof from a general shift in the way that society views the world; if they had not moved they may not have survived.

WHERE TO FROM HERE

The legal profession was quick to recognise the shift in commercial orientation that was occurring in New Zealand in the early 1980s; and we suspect that the major shift in orientation occurred prior to the 1985 survey. Since then, when the legal profession was markedly at the competitive end of the professions, attitudes have not moved to the same extent as those of the other professions surveyed. Indeed, attitudes towards competing on money matters have even moved against the general trend towards open competition. This lack of net change from 1988 suggests that the trend towards more favourable perceptions of advertising and competition by members of the legal profession may, in the medium term, have run its course.

The advertising styles that are presently used by legal practices appear to cover virtually the entire range of sensible possibilities for a serious professional service. In view of the attitudes of members of the profession that this series of surveys has documented, it is arguable that control of advertising style and content should cease to be an issue for the profession .... that such control as is necessary is adequately provided by law and the codes of practice of advertising agencies and media owners. ❑

FOREIGN INVESTMENT IN NEW ZEALAND

Mark A. Fox, Lincoln University and Gordon R. Walker, Canterbury University School of Law

investigate the myths about the extent and origin of foreign investment

INTRODUCTION

Foreign investment was an issue in New Zealand's first Mixed Member Proportional Representation (MMP), election held on 12 October 1996. The Alliance and New Zealand First, two of the parties which achieved a significant number of seats in the new parliament, are opposed to present levels of foreign investment. In a 120 member parliament, the breakdown of seats per party was as follows: National (44); Labour (37); New Zealand First (17); Alliance (13); ACT New Zealand (8) and United (1). This means that National or Labour will require coalition partners to form a majority government. It is highly likely that New Zealand First will be represented in either a right or left-wing coalition government. The Alliance would only feature in a left-wing coalition government. On any scenario, however, a senior coalition member (National or Labour), with liberal views on foreign investment will be pressed by a junior coalition member to amend present policy as expressed in the Overseas Investment Act, 1973-1995 (Act), and the Overseas Investment Regulations, 1995 (Regulations). The matter is complicated by the way in which immigration and foreign investment policy were conflated in the 1996 election campaign. We suggest that fact patterns involving immigration and foreign investment are best viewed as immigration questions (for example, business immigration). If there are abuses associated with immigration and foreign investment, then this a question that immigration policy makers should address. As to foreign investment, the key point to note is that New Zealand has always been a net capital importer and sought to attract foreign investment for growth: see K. McConnell and G Walker, "Foreign Direct Investment in New Zealand" in G Walker and B Fisse, eds., *Securities Regulation in Australia and New Zealand* (1994), 191-216. This Note examines recent data on foreign investment in New Zealand. In light of the election debate, some of our findings are eye-opening.

THE DATA

Our data was assembled, collated and analysed from figures provided over recent years by Statistics New Zealand and the Overseas Investment Commission.

TOTAL OVERSEAS INVESTMENT IN NEW ZEALAND

Table One summarises data relating to foreign investment in New Zealand as at March 1995. These data indicate that the three major sources of all foreign investment for New Zealand are: Australia (18.7 per cent); other Asia-Oceania countries (18.0 per cent); and the US (17.7 per cent).

Table 1
Foreign investment in New Zealand as at 31 March 1995

Source	$ millions	%
United Kingdom	6,779	7.0
Australia	18,118	18.7
U.S.A.	17,127	17.7
Canada	1,189	1.2
Japan	3,881	4.0
Other EU	2,954	3.1
Other OECD	1,178	1.2
Asia-Oceania	17,394	18.0
Other	28,107	29.1
Total	96,727	100.0

Source: Statistics New Zealand, *Hot Off the Press* (May 1996).

Table Two summarises foreign equity investment in New Zealand where direct investment means the acquisition of 25 per cent or more of the equity of the enterprise and portfolio investment is any investment in long-term bonds and equities which is not direct investment. Table Two demonstrates that direct investment has increased from $8.4 billion in 1989 to $32.4 billion in 1995, an increase of some 285 per cent. Furthermore, portfolio investment shows a small overall increase over the 1989-95 period from $1.4 billion to $1.7 billion, an increase of 25 per cent.

THE OVERSEAS INVESTMENT COMMISSION

The Overseas Investment Commission (OIC) administers the Act and Regulations. The OIC comprises two appointees of the Minister of Finance, one appointee of the Governor of the Reserve Bank and one appointee of the Secretary of Commerce. The functions of the OIC are specified in s 9 of the Act. Broadly, they comprise the consideration of proposals for overseas investment as defined and the provision of advice to the Minister of Finance. Section 9(1)(d) of the Act states the policy expectations flowing from the advisory function: "To advise the Government on such means as will ensure that the fullest possible benefit from overseas investment will accrue to New Zealand in promoting economic growth and development by the efficient utilisation of resources, and the highest degree of production, trade and employment". Note the link between overseas investment and economic growth in the OIC's advisory function.

Ownership of New Zealand land by foreigners was one salient issue in the lead-up to the 1996 election. It is worth noting how the Act and Regulations deal with real estate acquisitions. Regulations 8 and 9 specify transactions involving the acquisition of land that require or do not require consent from either the Minister of Finance or the Minister of Lands. Where consent is required under R. 8, the criteria for consent are contained in s 14A of the Act. Consent shall be granted only if the following criteria are met:

1. business experience and relevant acumen;
2. financial commitment;
3. good character; and,
4. where the investment relates to land, the national interest.

The content of the national interest criterion is further defined in s 14A(2)(a)-(e). It includes, for example:

1. the creation of new job opportunities;
2. the introduction of new technology or business skills;
3. the development of new export markets or increased export market access;
4. added market competition, greater efficiency or productivity; and
5. increased processing in New Zealand of New Zealand's primary products.

What is striking is the explicit link with economic growth in New Zealand and the implicit cost-benefit analysis. Section 14A(2) implies that land will not be sold unless the sale will result in economic growth for New Zealand and benefits exceed costs. Curiously, this is virtually identical to the policy of New Zealand First.

If New Zealand First were to rethink its policy, it would draw much comfort from a publication by one of the foremost thinkers in this area, DeAnne Julius: *Foreign Direct Investment: The Neglected Twin of Trade* Group of Thirty Occasional Paper 33 (Washington DC 1991). Julius points out that foreign investment stimulates trade. Given New Zealand First's desire for an export led recovery, we may yet see some revision of policy on this point.

More pertinently, however, there is a good domestic precedent for revamping and extending the national interest criteria in s 14A(2). This is found in the Commerce Commission *Guidelines to the Analysis of Public Benefits and Detriments in the context of the Commerce Act* (1994). A public benefit under ss 61 and 67 Commerce Act 1986 is synonymous with benefit to the public of New Zealand and hence with the national interest under s 14A(2). The *Guidelines* note that capital inflows are not themselves benefits to New Zealand. There must be a net gain in social or economic terms. Likewise transfers of wealth are not net gains, nor is job creation (although there may be some net benefit where the long term unemployed are concerned). In short, the Guidelines represent cogent thinking on public benefit which challenge aspects of s 14A(2) such as the creation of new job opportunities. They deserve careful consideration in any reassessment of foreign investment policy.

Table Three presents data relating to applications made to the OIC for the years 1991 to 1995. Over this period 1,866 consents were granted by the OIC, averaging $17.4 million each. Of the consents granted, 701 were for land sales. In total 241,206 hectares were involved in these sales, ie., 0.89 per cent of New Zealand's land mass.

Table Four shows country of origin data for those applications approved by the OIC between 1992 and 1995. These data show that 33.1 per cent of the dollar value of all applications was from Australians; 22.4 per cent was from the United States; 13.0 per cent from the United Kingdom and 9.6 per cent from Canada.

OVERSEAS INVESTMENT AND EMPLOYMENT IN NEW ZEALAND BASED COMPANIES

Table Five shows data relating to economically significant enterprises (those with greater than $30,000 annual GST expenses or enterprises in a GST exempt industry). Several important observations can be made from these data:

1. 97.2 per cent of these enterprises have less than 1 per cent overseas equity, and 80 per cent of full-time equivalent employees (FTEs) work in these enterprises;
2. only 0.5 per cent of economically significant enterprises have 25 per cent or more overseas equity; and
3. enterprises with 25 per cent or more overseas equity tend to employ significantly more people than do enterprises with less than 25 per cent (for example, enterprises with less than 1 per cent overseas equity typically employ 5.4 FTEs), whereas enterprises with over 50 per cent overseas equity typically employ 51.3 FTEs.

The above data shows that overseas investment tends to be in larger companies. Hence, it is not surprising that there is a high incidence of foreign ownership among companies listed on the New Zealand Stock Exchange and those that are in the Management Top 200 (ie., the largest 200 New Zealand companies in terms of turnover). A study conducted earlier this year, which examined overseas control of NZSE companies, indicates that 47 per cent of listed companies are foreign controlled, compared to only 17 per cent in 1985: see M Fox and G Walker, "Overseas Control of NZSE Listed Companies" (1996) 14 C&SLJ 324. A forthcoming paper by the same authors, which examines overseas control of the Management Top 200, shows that 39 per cent of these companies were foreign controlled as at December 1995.

CONCLUSION

The data presented confirms New Zealand's historical position as a capital importing nation and the identities of its principal providers of investment – Australia, the United Kingdom and the United States.

Concerns over foreign investment eroding New Zealand's sovereignty in terms of control over its land appear exaggerated in light of the statistics which indicate that less than one per cent of the land mass fell under foreign control in the period under scrutiny. In any event, concerns over the sovereignty of New Zealand's land per se need to be viewed in light of the potential benefits for New Zealand of foreign ownership, as stipulated by s 14(A)(2) of the Act.

The 285 per cent increase in direct equity investment in the 1989-95 period can be regarded as a positive vote for economic reform in New Zealand. As one commentator states, New Zealand has moved from one of the "... most regulated societies in the free world to [arguably] the world's freest market economy". S. Passow, "New Zealand: An Economic Turnaround Lays the Foundation for Investment" (1992) 26 *Institutional Investor* 5. This increase can also be seen as a vote of confidence in New Zealand by the global financial markets: see G. Walker and M. Fox, "Globalization: An Analytical Framework" 1996 3 *Indiana Journal of Global Legal Studies* 375. Finally, the data suggests that foreign investment may have positive impacts for employment and job creation in New Zealand.

Table 2
Foreign equity investment in New Zealand companies
($ millions)

	1989	1990	1991	1992	1993	1994	1995
Direct investment	8,412	12,293	13,294	17,750	21,364	27,891	32,368
Portfolio investment	1,378	1,561	1,766	850	2,468	1,581	1,723
Total	9,790	13,85	415,060	18,600	23,832	29,472	34,091

Source: Statistics New Zealand, *Hot Off The Press* (1995, 1996).

Table 3
Overseas investment commission activity figures, year ending 31 December:

	1991	1992	1993	1994	1995	1991-95
All transactions						
Total applications processed	248	220	286	279	382	1,415
Total consents granted	335	343	382	362	444	1,866
Total considerations ($m)	$6,300	$6,740	$9,409	$5,226	$4,877	$32,552
$m per consent granted	$18.8	$19.7	$24.6	$14.4	$11.0	$17.4
"New" investment consents granted	241	241	na	264	332	
Percentage total	72%	70%		73%	75%	
Total considerations ($m)	$4,549	$5,229	na	$2,593	$2,871	
Percentage total	72%	78%		50%	59%	
$m per new consent granted	$18.9	$21.7	na	$9.8	$8.6	
OIC land sales						
Consents granted	90	103	114	162	232	701
Percentage of total consents	27%	30%	30%	45%	52%	38%
As a percentage of total farm sales	2.6%	2.4%	2.8%	4.5%	7.3%	3.8%
Area (hectares)	41,896	29,991	48,997	58,650	61,672	241,206
As percentage of forested and farmland	0.20%	0.14%	0.23%	0.27%	0.28%	1.13%
As percentage of NZ land	0.15%	0.11%	0.18%	0.22%	0.23%	0.89%
Hectares per consent granted	465.5	291.2	429.8	362.0	265.8	344.1

Source: Overseas Investment Commission

Table 4
Overseas investment commission,
Approved applications by country of origin, 1992-95

	Value ($ millions)	%	No		Average ($ millions)
Australia	8,693	33.1	313	20.4	27.8
United States	5,881	22.4	348	22.7	69.9
United Kingdom	3,423	13.0	192	12.5	17.3
Canada	2,515	9.6	36	2.4	7.3
Hong Kong	1,712	6.5	99	6.5	11.2
Japan	867	3.3	118	7.7	17.8
Singapore	1,416	5.4	127	8.3	16.9
Other	1,746	6.6	298	19.5	5.8
Total	26,252	100.0	1,531	100.0	17.2

Source: Overseas Investment Commission.

Table 5
Enterprises and full time equivalent persons engaged by degree of overseas equity

Overseas equity	Enterprises		Full-time equivalent employees (FTEs)		FTEs/ Enter-prise
	No	%	No	%	
Less than 1%	187,523	97.2	1,010,453	80.0	5.4
1-24.9%	973	0.5	27,518	2.2	28.3
25-49.9%	491	0.3	25,842	2.0	52.6
Over 50%	3,884	0.2	199,161	15.8	51.3
Totals	192,871		1,262,974		6.5

Source: Statistics New Zealand, *Business Activity Statistics* (1995)

ASSAULT ON THE EARHOLE

Ross Burns

detects moves towards a modern doctrine of self-defence in a technological age

Bullerton – CA 163/92 – was an appeal from the District Court at North Shore. The appellant had been convicted of an offence under s 188 Crimes Act 1961, of causing grievous bodily harm to a man referred to throughout the proceedings as F.

For a period of some months in 1991, B had been receiving obscene telephone calls from F, of whose identity she was unaware. The calls consisted mainly of heavy breathing although there were occasions when F made indecent suggestions to B involving consensual activity with farmyard animals.

Telecom had been unable to prevent the calls and an attempt by police to trace the caller had foundered when it was discovered that the calls were being made from a number of public telephone boxes.

B had no alternative other than to change her telephone number and she was reluctant to do this as she was a self-employed relief worker and risked the loss of some of her regular custom.

She decided to act. With the help of a friend who was an electronics engineer she devised what was described throughout the trial as a "screech-box". When next F telephoned, the screech box was activated and a literally ear-piercing sound was transmitted down the line. So loud was the sound that F was partially deafened in one ear, and now suffers from severe tinnitus.

F complained to the police, and B was interviewed. She admitted using the screech box, and said to the police (and later repeated to the jury) that "it served him bloody well right".

She was convicted and appealed. The ground was that the Judge in the District Court had been wrong to withdraw self-defence from the jury.

The Court of Appeal judgment repeats the facts previously outlined and then continues as follows:

"On the appellant's behalf it was argued with considerable tenacity by Mr O'Laggin that she was exercising a lawful right to defend herself, and that the jury should have been allowed to consider that defence. Mr O'Laggin's florid vocabulary, categorising the appellant's actions variously as "pre-emptive strike" and "attempted pesticide" were not helpful to the debate, but one cannot gainsay the force of his legal argument. It may usefully be summarised by posing two questions. First, if I, the recipient of obscene calls, reasonably believe that the continuation of these calls would lead to psychological distress, as well as the inconvenience of having to change telephone numbers, am I not entitled to use reasonable force to prevent that result? And if my belief was that the force that I used would cause only discomfort, can that be said to be other than reasonable ?

"In our view the question raised is one of great importance. Is a citizen entitled to defend herself against psychological and emotional attack by physical means, or must she reply only in kind?

"We are in no doubt that the appellant would have been entitled to use psychological retaliation. If she had, for example, hurled F's obvious inadequacies back in his face, we would have had no hesitation in allowing this appeal. Indeed, such a response does not constitute an assault and we doubt that matters need have troubled the Courts. But here there was an application of what we unhesitatingly agree to be physical violence in anticipation of psychological harm.

It is trite law that one need not wait until one is struck before defending oneself. If one anticipates physical harm, one may take reasonable steps to prevent it. Of course, such steps must not be more than reasonable, although one is not expected to judge them to a nicety. The "proportionality" principle is well enshrined in the law of self-defence.

We accept that the force that the appellant used was no more than she believed to be necessary to prevent harm to herself from occurring. But we feel constrained to agree with the Judge below that physical force may not be used to prevent psychological harm. Like must be met with like. That is of the essence of self-defence. Our attention was drawn to a number of authorities but none sums this principle up more pithily than the short judgment of the High Court of Australia in *Smilovici v DPP of NSW* (54 NSWLR 649)

> and we agree that the law does not permit a man to break another's jaw merely because his chatter was interfering with good drinking time. The natural sympathy felt for the defendant is best reflected in the imposition of a discharge without conviction, as properly occurred in this case.

But that does not dispose of the matter. Another purpose of the appellant's assault upon F was to prevent the necessity of changing her telephone number. While a citizen's home is no longer her castle, and may be intruded upon almost at will by various servants and agents of the Crown, she remains entitled to enjoy her property without interference from others. The law recognises the right to defend property. F's action would have deprived the appellant of her property – her telephone number – and she was entitled to use reasonable force to protect it. And it may well have been that a jury would have found that she did no more than that. She was entitled to have this defence put to the jury, but because of the Judge's ruling it was not. In the circumstances we must allow the appeal." ❑