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DECLARING THE LAW

Litigation currently before the German Federal Constitutional Court gives an insight into the true meaning of the much derided declaratory theory of the common law.

The authorities in Germany have decided to alter the spelling of the German language in several respects. The distinctive ß character is to go, to be replaced by the more mundane "ss". The spelling of certain other words is to be regularised, with the result that their etymology will be obscured.

There have been numerous protests and now there is litigation in an effort to halt the changes. Meanwhile the education system has started to implement them. The new spelling rules are defended on the wearily familiar grounds that they are more equitable, presumably because they reduce the distinction between the intelligent and the unintelligent.

In France there is also a centralised state body, the Academie Française which regulates, or attempts to regulate, French vocabulary and spelling. It has the merit of being composed of literary people rather than bureaucrats, but nonetheless in the end it pursues a state policy, the maintenance of the distinctiveness of the French language. The language is treated as an instrument to be used in the pursuit of the political goal of national consciousness.

Now contrast this with the way in which English spelling and usage is determined.

A number of different dictionaries are produced, each with its own editor. As it happens, this activity takes place in the private sector. Nothing of principle hangs on that, but it probably explains how the system has survived. Had there been a state monopoly it would have been captured by some interest group or bureaucracy by now.

And how do the editors of dictionaries determine spelling? The answer is that they examine usage, poring over the written language in particular. Thus they detect, and declare, that "develope" is archaic and "develop" more normal.

This is the true analogy with the common law, not the caricature commonly presented in teaching and epitomised by Lord Denning's "fairy tale" that there was something called "the law" with an independent existence of which Judges were the High Priests.

Far from being an anointed priesthood, the role of Judges in the common law system is a relatively humble and perhaps unexciting one. It is to determine what the parties to transaction intended in particular cases and what is accepted best practice in general. Their task is then to declare and ratify it.

In contrast Judges in the Roman Law world deal with a law that is handed down from on high by the state. Like all such monopoly institutions, it is then liable to capture, or to becoming regarded as a mere instrument of policy. And in the common law world, the increasing use of legislation in the private law has led to the belief that Parliament is entitled to "change the law" in pursuit of social goals. It is a short step then to believing that Judges can do the same. Since law comes from on high, it may as well come from Judges as from Parliament. This is the stage of thinking that we now seem to have reached.

The analogy with dictionaries provides another lesson. Because there are several private sector dictionaries, and the field is contestable, editors are forced to produce the most useful and accurate dictionaries, not ones which deliberately alter spellings or meanings in pursuit of some social policy. Thus dictionaries record, not lead, the increasing "gender-neutralisation" of language, though it should be pointed out that this is mainly driven by the public sector.

It is no accident then that the heyday of the common law was the period when there were in England four competing Courts each ever-ready to take a slice of another's jurisdiction. Since the foundation of New Zealand however, a legislated monopoly has been trading on that reputation with predictable results.

If today it were proposed that spelling be regularised by Act of Parliament this would be seen as a ludicrous example of Parliament interfering with matters it had no right to interfere with, whatever the doctrine of parliamentary sovereignty might say.

But this proposal is no more ludicrous than that the meaning of words like "marriage" be altered by law in pursuit of social goals. We are simply accustomed to the idea that marriage is regulated by the state and spelling is not.

The lessons are clear. We, the people, are the real authorities and the job of the "authorities" is to determine our views. This is not to be done, however, through the political process which consists largely of gestures the costs of which are concealed. It is to be done by examining what we actually do day to day in decisions in which we are faced with opportunity costs.

This evolution of law can be seen happening in the People's Republic of China where, so far as there is any law, commercial law is largely the result of standard forms emerging from practitioners. Meanwhile a committee of bureaucrats labours away in Beijing to draft codes of company and insolvency law, years behind what is actually happening in the real world.

It is also apparent that a better result comes from having a diffused network of "authorities" rather than a monopolistic and hierarchical authority.

This is true of all our social institutions, including our fundamental institution, the law. ❑

PARTNERSHIP

Warren Allen, management consultant, Wellington

analyses issues we often take for granted

All practising lawyers operating in partnership work together in an intimate business relationship.

The relationship creates unique dynamics of its own and from many points of view – personal, financial, business and management. Yet I suspect most lawyers who are in partnerships or are intending to enter one never give any real thought to all the business ramifications. As a result there can be painful consequences which in some cases can become extremely costly if not fatal.

Partners are involved in a business venture. The vital core of that business is the partners and their relationships to each other. Of course in most partnerships – until they become very large – there is a personal friendship between all the partners and that is important. But to regard the partnership as akin to a marriage partnership and based primarily on emotional factors such as liking, respect, mutual interests etc is to run the danger of putting the business at risk.

How many partnerships have a written Partnership Deed which sets out the main elements of their business relationship? How many partnerships have a Job Specification for a partner so that the existing and future partners know precisely what is expected of them? How many partnerships strategically plan for the taking in of new partners? How many partnerships have worked out any formal exit path for older partners? How often is the profit share system re-examined to see whether it is still fair to all concerned? How is partner performance assessed? Have the partners agreed on common aims and aspirations to establish the culture of their firm? Has the partnership a Strategic Plan; or a Business Plan? Are these being implemented?

I suspect in many cases the answer to most if not all of these questions is in the negative.

Over the last two decades much greater attention has had to be given to many of the business aspects of practice. This has largely taken the form of employing professional people to look after administration, marketing, human resources, technology and finances. It was realised that matters such as work-in-progress control, credit control, client service, good staff relations, up-to-date technology etc etc were necessary if not for survival then at least for enhanced efficiency and profitability.

But the corner-stone of the business, its very essence – the partnership relationship – has remained curiously and largely unattended. Why? I guess because it is all too hard and a bit messy. Most human beings actually don't like embarrassing or conflict situations or doing anything that hurts another – particularly someone with whom they have a relatively close relationship. And thus it's understandable that partners are often not comfortable with matters such as partner assessment, altering the profit share system, dealing with the persistently under-performing partner and all the other difficult issues. Of course some have and in most cases their business has benefited.

While professional managers have been successful in most areas of legal firm business, they do find one area which they can't really manage for the partners – the partnership issues. It is in this area that partners retain control and accordingly where only they can take the appropriate action. And of course they are the very issues which are so vital to the long-term health and prosperity of the business – entry and exit of partners, profit share, partner contribution/performance and the culture and direction of the firm.

A partner is:

- a lawyer (the professional hat)
- part owner of the business (the investment hat)
- a boss (the employer hat)
- a joint venturer (the partnership hat)
- a member of the firm (the corporate hat)
- an individual (the personal hat)

Each of these facets carries with it certain responsibilities. Thus the professional hat requires the partner to be not just another lawyer but a very good one. The ownership aspect carries with it not only the financial liabilities but also the responsibility to ensure that the business (investment) is retained as a viable operation and operating profitably. The boss hat requires the partner to show leadership qualities and to recognise that no employee is going to react favourably to the "do as I say, not as I do" approach; the partnership aspect in many respects is one of the most important because, as any party to a joint venture knows, the calibre of the other parties to the joint venture is vital. The corporate aspect is probably more important in larger firms which develop the view that the firm has been, is, and will be in existence as an entity in its own right despite comings and goings of individual partners. The personal factor cannot be understated. The partner has social relationships and commitments to spouse, children, parents or friends. Partners (and also the firm) should not jeopardise these relationships and owe it to themselves and those others to preserve their physical and mental health and secure enough leisure time.

The extent to which partners recognise these different facets and responsibilities and, perhaps more importantly, the extent to which they try to discharge the responsibilities will go a long way towards ensuring the success of the firm. Whilst the type of contribution that a particular partner can make to the firm will vary from individual to individual, there ought to be a fairly uniform level of commitment of all partners. Contributions may be different but they should be relatively equal otherwise dissatisfaction and dissension creeps in. Like rust in the steel frame of a building this will, if unchecked, lead to a collapse of the whole structure.

At the end of the day legal firms are business enterprises and have to remain competitive in an increasingly competitive world. The ultimate deciders of whether or not that happens are the partners. The firm (the business) will stand or fall on the calibre and efforts of the partners. ❑

RETIREMENT VILLAGES

D F Dugdale, Law Commissioner

asks for comment on the latest Law Commission discussion paper

The Law Commission has published a new discussion paper, *Retirement Villages* (NZLC PP 34). The principal concern of the paper is the protection of residents or intended residents of such establishments from financial risks. Such risks are likely to result, in the case of new developments, from the developer's reliance on the residents' own money to bring the (usually under-capitalised) project to completion. In addition the continued viability of every village is dependent on sound management skills which have not in every case in the past been in evidence. While following the collapse of schemes financiers in New Zealand seem to have been as a rule too good hearted or too squeamish to turn residents out into the snow, it is also the case that following such collapses residents have found themselves enjoying amenities less desirable on terms less advantageous than they had been promised.

Currently (though in some cases it depends on how you interpret the Securities Act 1978 s 5(1)(b) and the observations on contributory schemes of the Privy Council in *Culverden Retirement Village v Registrar of Companies* [1997] 1 NZLR 257) most retirement villages are subject to the provisions of the Securities Act, though it seems that only about a third of them acknowledge that this is so. The Securities Commission at present copes with its responsibilities by exempting retirement villages from the general Securities Act obligations but on terms that are really an attempt to reshape such obligations to the special situation of retirement villages. (The current exemption notice is the Securities Act (Retirement Village) Exemption Notice 1998 SR 1998/187.)

A valuable report commissioned by the Securities Commission and entitled "*Resident Funded Retirement Villages; proposals for the reform of the law*" was published in December 1993. That report recorded that the first preference of that task force of experts would have been "to establish legislation governing the regulation of retirement villages. Such a course of action would enable the establishment of a regulatory regime which is simple and clear and directly relevant to retirement villages and the special requirements which pertain to them". The task force assumed, however, that there were political difficulties in the way of new separate legislation and went on to consider alternative solutions. In the event those proposals remained unimplemented. It is such separate legislation as the task force preferred that the Law Commission now proposes.

Efficient trading in securities (if the writer correctly understands such mysteries) requires an accurate assessment of risk and the concern of such bodies as the Securities Commission is with obstructions to the flow of information needed for such an assessment. This is rather different from the concerns of residents or prospective residents of retirement villages whose purpose is not to gamble but to secure the roof over their heads that has been promised them.

Also the Securities Commission's focus is on the stage at which securities are marketed, while proper protection for residents of retirement villages to be effective must extend beyond the initial marketing stage to ongoing management.

For these sorts of reasons the tentative suggestion of the Law Commission is to replace existing arrangements with a system under which what are styled in the proposal "prudential supervisors" will settle the form of disclosure documents and be responsible as ongoing prudential watchdogs. The main surviving function of the Securities Commission would be approving the appointment of the prudential supervisors (trustee companies would be automatically eligible). The Securities Commission would also, along with the Registrar of Companies, have certain long-stop powers.

This approach makes it unnecessary in the statute and any delegated legislation to spell out in any detailed way the methods by which those marketing and operating retirement villages will satisfy their prudential responsibilities. Those duties will be settled in each case between the operator and the prudential supervisor. Because the proposed statute will expressly provide that prudential supervisors will be responsible to residents for breaches of their supervisory obligations causative of loss, the supervisors may be expected to take their duties seriously and impose conservative regimes. Such matters as audit and reporting obligations for example will be determined between the supervisor and the operator either in the original Deed of Appointment or pursuant to machinery contained in that document.

There will be a provision entitling residents to financial information in the hands of prudential supervisors.

The prudential supervisors will, of course, have to be paid, but under the scheme other compliance costs incurred at present will no longer be needed and it may reasonably be hoped that interested trust corporations will develop expertise that will mean that the incurring of unnecessary costs can be avoided. The statute will confer various powers on a prudential supervisor that can be exercised when it believes it has occasion to get worried about a situation. These will range from the comparatively innocuous one of summoning a meeting of residents to an application to the High Court for the appointment of a manager.

The Law Commission shares the view that retirement villages need prudential supervision, and that the law's present machinery is excessively cumbrous and not particularly effective. The proposal for a solution set out in the Law Commission's paper is no more than a basis for discussion and is no doubt susceptible of improvement. Submissions are invited before 28 February 1999. Any further inquiries should be addressed to Megan Leaf at the Law Commission, PO Box 2590, Wellington, Telephone (04) 473-3453 or Fax (04) 471-0959 or by e-mail to Megan Leaf@ lawcom.govt.nz. ❑

IN THE DISTRICT COURTS

Judge R L Kerr, editor of the District Court Reports

MEANING OF "AMPUTATION"

Judge G V Hubble, in *Dept of Labour v McFarlane Laboratories NZ Ltd* [1997] DCR 927 dealt with the prosecution of an employer whose employee was carrying out the process of mincing lengths of shark cartilage. The process required the employee to feed lengths of cartilage into a sink hole and then to auger approximately 230 mm down the hole.

There was no guard over the sink hole, and the employee, whilst forcing a piece of cartilage which had become stuck on to the auger, had his gloved hand come into contact with the auger which removed the tip of his left middle finger.

There was evidence from a specialist that the medical definition of amputation was "the cutting off, pruning or avulsion of a body part or tissue", avulsion having the dictionary definition of "a sudden tearing away".

The question was whether or not what happened to the employee came within the definition of "serious harm" contained in the First Schedule to the Health and Safety in Employment Act 1992. In that Schedule serious harm was defined (inter alia) as –

> "Amputation of body part".

The learned District Court Judge found there was an amputation, serious harm had occurred and fined the defendant $10,000, $6000 of which was to be paid to the employee.

There was an appeal to the High Court and Laurenson J in *McFarlane Laboratories NZ Ltd v Dept of Labour* (HC, Auckland, AP 292/97, 16 February 1998) upheld the District Court Judge's determinations.

The appellant submitted that notwithstanding the amputations were deemed to be serious injuries, a Court was still required to determine as a matter of fact and degree what amounted to an amputation. In short, it was inappropriate to simply accept a medical definition of the term.

The High Court Judge found that as the injured employee was unable to work for some seven weeks, and the tip of his finger would be likely to be desensitised for up to three years, there must be serious harm,

Further, His Honour referred to the long Title of the Act "An act to reform the law relating to the health and safety of employees, and other people at work or affected by the work of other people" and concluded the object of the Act was to prevent hazardous situations occurring in the workplace. His Honour said that defining "serious harm" was, amongst other things, to ensure that the Department of Labour became involved, not only to make an assessment of the situation, but more importantly to ensure that situations which created the incident were not repeated. The appellant had determined of its own volition that the harm to the employee was not serious and had not notified the department which the learned Judge decided was exactly what the Act sought to prevent.

Laurenson J determined that the District Court Judge was correct in accepting the medical definition of the injury as amounting to an amputation.

The fine, it was submitted, was manifestly excessive. The District Court Judge had applied the criteria set out in *Dept of Labour v De Spa & Co* [1994] 1 ERNZ 339. The Judge specifically emphasised the need for deterrence as being to the forefront in fixing penalty. Notwithstanding the appellant's submission that any such emphasis required an assessment of the degree of culpability or conversely the extent to which the appellant had sought to prevent accidents, the District Court Judge, it was found by the High Court, did not misdirect himself when determining the level of penalty, and in ascribing importance to the deterrent aspect.

Reference was made too, to *Fairfax Industries Ltd v Dept of Labour* [1996] 2 ERNZ 551 where Paterson J concluded there had been a gradual increase in the severity of penalties which increase was entirely appropriate. $10,000 was not manifestly excessive.

Laurenson J in considering whether or not a payment of $6000 to the employee was manifestly excessive, stated that the District Court was entitled to make an order, having seen and heard from the employee and therefore being able to assess the degree of injury and its effects.

SUMMARY PROCEEDINGS ACT ss 19B, 37, AND 204

Anderson J in *Police v Rowe* (HC Auckland, AP 256/97, 9 February 1998) dealt with an appeal by way of case stated from the District Court. An information sworn on 17 December 1996 by a constable alleging a drinking and driving offence was dismissed without prejudice to it being relaid, but because of lapse of time it could not be relaid.

At trial in the District Court the point was taken that the "on-the-spot" summons issued to the respondent was not correctly worded. Anderson J said that a s 19B summons provided a fast track procedure for a defendant to appear before Court. The section envisaged the signing by an enforcement officer and service on a defendant of a summons in the form prescribed. The prescribed form included alternative descriptions of offences, the inapplicable description to be deleted to leave extant the description appropriate to the case. One description concerned particulars of offences for adult offenders, and the other for persons under 20 years of age who commit an offence when driving with a lesser amount of alcohol in their breath.

The enforcement officer deleted the description for an adult offender leaving the alleged offence as though the respondent was under age, although he was over age.

The case stated required determination of whether the error was a "defect, irregularity, omission or want of form", as those words were used in s 204 of the Summary Proceedings Act, and more particularly in terms of that section, whether there had been a miscarriage of justice.

Anderson J referred to a judgment of the Court of Appeal *R v Blackmore* [1994] 1 NZLR 268, 272 where the Court referred to questions of miscarriage of justice and nullity (from s 204) as often tending to merge. His Honour went on to say in view of the relevance of degree each case required a subjective evaluation, the purpose of an impugned document being relevant in the evaluation process.

His Honour found that the error was no more than a defect or irregularity such as would in the absence of the Court being satisfied that there had been a miscarriage of justice, be preserved by the operation of s 204. He referred specifically to the fact that the defendant answered the summons, appeared in Court, there only subsequently being an argument as to the validity of the summons.

On appeal, the respondent took the point that the notice of appeal had not been signed by a constable as required by s 37(3) of the Summary Proceedings Act, but by a solicitor employed by the Police. Anderson J determined the practical position was that even if the form of signing was a defect, irregularity, omission or want of form, it would nevertheless be saved by the operation of s 204, and accordingly there was no need to determine whether the signature by other than a constable invalidated the notice of appeal.

HARASSMENT ACT 1997

Giles J had to determine in *O'Brien v Police* (HC Auckland, R 216/98, 13 August 1998) whether when a defendant appeared on two charges of injuring with intent under s 189(2) Crimes Act 1961 (the Act), a District Court Judge had jurisdiction to consider bail, if the defendant had previously been convicted of an offence under s 189(2).

Section 318 of the Act defines what are called "specified offences". In particular it defines as a specified offence –

"Section 189(2) injuring with intent to injure."

The point for consideration was where a conviction was entered under the second limb of s 189(2) ie with reckless disregard for the safety of others injures any person, that offence comes within the description given in s 318 of specified offences. The Judge referred to *Hansard* and the debate on the section and commented that it could be seen the primary focus of the legislature was the need to protect the public, which was to be achieved by limiting bail rights for those with a history of violent offending.

His Honour said violent offending clearly incorporated all of the offences covered by ss 188 and 189 of the Crimes Act, and accordingly although the second leg of s 189(2) was not referred to specifically, was satisfied that the legislature clearly intended it to be covered.

In support of that, His Honour referred to s 188(1) which makes it an offence to –

(a) Cause grievous bodily harm by wounding any person;
(b) Cause grievous bodily harm by maiming any person;
(c) Cause grievous bodily harm by disfiguring any person,

but in s 318 there is simply reference to wounding with intent to cause grievous bodily harm. If the argument for the appellant was to be upheld, then maiming or disfiguring would not be a specified offence.

SECTION 318 CRIMES ACT

The Harassment Act is a new statute and is starting to be used in the District Court for the purpose of obtaining restraining orders.

In July of this year, Judge C M Shaw issued two judgments under the Act.

In *LMP v GRCH* (tbr in DCR) Her Honour pointed out that the Act did not provide for set procedures to be followed in hearing an application.

In the absence of any clear direction she considered the procedures adopted must be sufficient to ensure that both parties obtain a fair hearing, that the interests of justice were met and that the object of the Act of providing protection for victims of harassment was not frustrated by the process.

She indicated that the application of those principles should ensure that the procedure for each hearing could be regulated according to the nature of the application, the type and amount of material filed in support and opposition, whether the parties were represented by counsel, whether the application was opposed, and in the light of anything else brought to the Court's attention. She commented that at one end of the scale an unopposed application disclosing adequate grounds on the papers could be dealt with (in some circumstances) without the need of a hearing.

At the other end a fully contested application could require full cross-examination on the affidavits filed. Variations of approach between the two extremes might be dictated by the circumstances. It was necessary, however, that the parties were never in a domestic relationship.

The learned Judge found that the respondent's act of writing letters to the applicant amounted to harassment. That harassing behaviour threatened to cause the applicant distress, and a reasonable person in the applicant's position would be threatened in the same way. The applicant on occasions was distressed.

In the circumstances then because of the way in which the respondent behaved, and more specifically because of the number of letters and their content, the learned Judge determined that a restraining order should be made.

However, in *Chong v Gatehouse* (tbr in DCR) no restraining order was made. The Judge found that there was no love lost between the parties, and eye contact between them was not of a friendly variety. However, where there was eye contact, that contact was fleeting and was in public.

The learned Judge commented that the Act, and more specifically the provision relating to issue of restraining orders, must be interpreted with a degree of common sense. She considered that the object in s 6(1)(b) of ensuring that there was adequate legal protection for all victims of harassment would not be advanced by the making of restraining orders in cases where two parties exchange angry glances because of ill feeling between them.

An order was declined.

S 9 SERIOUS FRAUD OFFICE ACT

In *R v Ross* (tbr in DCR) Judge P J Keane was required to rule on whether or not a tape recorded interview of one of the accused was admissible through a Crown witness. At the time of argument the accused had not indicated an election of whether to give evidence, and the prospect that he might not could not be ruled out.

The Crown opposed the application to admit the interview because by admitting it the accused would enjoy the advantage of putting his case by effectively giving unsworn evidence but even more specifically, because the interview was conducted under s 9 Serious Fraud Office Act, the use to be made of the interview being governed by ss 26 and 28, the accused was barred from using the interview, it only

being available to be admitted if the Crown used it in cross-examination on the grounds of prior inconsistency.

The accused argued that s 9 created a limited immunity or privilege, with an ability to waive that immunity or privilege. The learned Judge concluded that the statement contained exculpatory and inculpatory material. Certain inculpatory acknowledgements which he made could be capable of being met and may well have been met by evidence called by the Crown. But the fact that the accused made them did something to strengthen the Crown's case.

The Judge determined that the statement was truly a mixed statement of inculpatory and exculpatory material, and accordingly ruled that the contents of the tape might be played to the jury, the accused having the ability to waive such privilege or immunity as he might have had.

S 107(1) SUMMARY PROCEEDINGS ACT

In *Nuplex Industries Ltd v Auckland Regional Council* (High Court, Auckland, AP 163/98, 23 September 1998), the appellant had been charged with an offence under the Resource Management Act 1991. In the District Court, counsel for the appellant objected to the admissibility of evidence given by an officer of the respondent. The learned trial Judge conducted a voir dire and ruled that the challenged evidence was admissible. The appellant gave notice of appeal by way of case stated.

Two matters were raised by the High Court. They were –

- Whether the Court had jurisdiction to hear what amounted to an appeal in respect of an interlocutory matter, and
- Whether the case stated was in proper form.

On the first question the Court referred to *Black v Fulcher* [1988] 1 NZLR 417 and dicta of Cooke P at 420 –

> In the summary criminal jurisdiction interlocutory general appeals are not provided for. As to points of law, similarly s 107 of the Summary Proceedings Act requires the determination of an information or complaint before an appeal lies.

The Court applying that dicta held it had no jurisdiction to hear the appeal and accordingly dismissed it.

The second question concerning the form of the case stated was considered. Section 107(3) of the Act was referred to, and more specifically observations of Henry J in *Conroy v Patterson* [1965] NZLR 790 at 791 (and the comments bear repeating) –

> Summary Proceedings Regulations 1958 (SR 1958/38) ... now prescribe form 35 which specifically requires the grounds of determination to be set out in the case itself ... The form ought to be followed. The form may not make it altogether clear that the question of law must be specified but s 107(3) does. ... The Supreme Court is entitled to know with sufficient precision what was the question of law, what were the established facts relevant to that question; and what were the grounds for determining the question of law in the manner in which it was determined. *The Supreme Court should not be asked to ferret around among the notes of evidence and the judgment in the Case to see just what was determined either as a matter of law or fact.* Those matters so far as they are material to the appeal ought to be sufficiently stated in the Case itself. (Emphasis added.)

What had happened in *Nuplex* was that the judgment of the District Court Judge had been annexed as part of the Case on appeal, without the question of law to be decided being identified and without the facts found by the Judge being specified.

Had the first question been answered in favour of the appellant, then the Case would have been remitted to the District Court for correction.

It was insufficient for a Judge to refer to some findings and then refer reasons for judgment to the High Court for the remainder of the findings to be located by that Court.

A MATTER OF TRIVIA

A decision *R v R* [1998] DCR 432 was not reported with an exchange between the trial Judge and counsel for the accused (Mr T A de Cleene). The exchange, with counsel for the accused a former member of Parliament, shows how a slip of the tongue can suddenly be transformed into a matter of some amusement –

Judge Lance QC:	Mr de Queen submitted ...
Mr de Cleene	... point of order Your Honour
Judge Lance	Pardon
Mr de Cleene	Point of order
Judge Lance	Mr de Cleene this is but the District Court, not the debating chamber you have mistaken the forum ...
Mr de Cleene	Quite so, Your Honour, quite so but my point is the same ... and I want the record to show that although I was right behind the Honourable Fran Wilde ... upon reflection I will retract that ...
Judge Lance	You could not be seen Mr de Cleene?
Mr de Cleene	Oh no – I fully supported her ... and that may be a doubtful position also ... in any event I was a member of Parliament that introduced the Homosexual Law Reform Bill ...
Judge Lance	And supported its passage Mr de Cleene?
Mr de Cleene	Quite so, sir, indeed to the hilt ... and it is necessary for me to say, and for the record, I am not and never have been a homosexual and Your Honour's reference could, if unchallenged, infer otherwise
Judge Lance	Well, thank you Mr de Cleene, I can assure you that if this decision is ever reported your firm stance will be recorded, unexpurgated, which may go some way to relieve your concern and remedy my error – now can we proceed?
Mr de Cleene	Your Honour, Erskine once said ...
Judge Lance	Some other time perhaps Mr de Cleene. ❑

The Editor offers a free subscription for one year to NZLJ to the first reader who can tell us what Erskine did say.

THE PROPOSED PPSA

D F Dugdale, Law Commissioner

discusses aspects of the draft Bill. The first part of this paper was delivered to a Legal Research Foundation symposium on 18 August 1998

FAILURE TO PERFECT

The personal property securities regime proposed by the Law Commission in 1989 (*A Personal Property Securities Act for New Zealand* NZLC R8) contemplates the existence of a register that in the case of motor vehicles will as under the Motor Vehicle Securities Act 1989 be based on registered numbers and in other cases a nominal index. A security will be perfected either by possession (as in a pledge) or by registration of notice of the existence of the security. An unperfected security interest is subordinated to the rights of a buyer or lessee for value without notice and to a subsequent security interest. There is no argument about any of that.

What is controversial is that under the Commission's proposal an unperfected security interest binds the parties inter se even as against such persons claiming under the debtor as judgment creditors, official assignees in bankruptcy and liquidators. The Commission's report notes that its advisory committee was almost evenly divided on this issue (p 12). This part of the Commission's proposal departs from the various North American models on which the Commission's proposal is based. Currently of course the Chattels Transfer Act 1924, s 18, and the Companies Act 1955, s 103(2), have an effect contrary to that proposed for the new statute.

An explanation of the solution favoured by the majority of the advisory committee requires a return to first principles. There are two classes of persons who may be misled and suffer loss as a consequence of A being in possession of goods that he does not, in fact, own, namely –

- A's general creditors who may extend him credit or forbearance as a result of drawing from the fact of A's possession of the goods a mistaken conclusion as to his financial substance; and
- those to whom A may purport to sell or mortgage the goods.

Protection of the first of these two classes, the general creditors, should not be a purpose of the proposed legislation.

The policy of the first English Bills of Sale Act of 1854 was to protect general creditors. This is clear from the preamble.

> Whereas frauds are frequently committed upon Creditors by secret Bills of Sale of personal Chattels, whereby persons are enabled to keep up the Appearance of being in good Circumstances and possessed of Property and the Grantees or Holders of such Bills of Sale have the Power of taking possession of the Property of such Persons to the Exclusion of the rest of their Creditors ...

Under that statute and its successor of 1878, therefore, unregistered bills were void as against trustees in bankruptcy and execution creditors.

This approach was consistent with the policy of a provision which had been included in English bankruptcy legislation since 1624 to the effect that the assets available to a bankrupt's creditors were not only those which he owned, but also chattels in his possession in such circumstances that he appeared to be their owner.

The first New Zealand Bills of Sale statute was enacted in 1856 and faithfully followed the English Act of 1854. The subsequent history of the legislation is too complex to describe on the present occasion otherwise than in broad outline. It is sufficient to note that it was relatively late in the day that protection of specific disponees rather than general creditors against unregistered instruments was introduced, in 1868 in relation to purchases of stock, in 1889 in relation to purchases of wool and crops, and in 1922 in relation to other purchases and to subsequent encumbrances. In 1924 a large hole was made in this protection by the invention of the customary hire purchase agreement.

New Zealand bankruptcy law contained a reputed ownership provision until the Bankruptcy Act 1908, s 61(c), was repealed and not replaced by the Insolvency Act 1967.

As to companies in the United Kingdom it was in 1900 that there was first enacted the requirement for public registration of mortgages or charges created or evidenced by an instrument which if executed by an individual would require registration as a Bill of Sale. This was copied in New Zealand in 1903. The policy of the provision was the protection of general creditors by publicising the company's financial position, and consistently with this, failure to register made the security ineffective as against an execution creditor or liquidator (Companies Act 1955, s 103). In addition, since the enactment of the Chattels Transfer Act 1924, s 4, all persons are deemed to have notice of a registered security granted by a company wholly or partly upon chattels.

It is clear that the protection of general creditors is one purpose of the North American provisions. So para 9 of the Official Comment on Art 9-301 of the US Uniform Commercial Code states:

> The rules for the subordination of unperfected security interests have a purpose – in common with similar rules in all filing and recording systems – to impose sanctions for not adhering to filing or registering requirements. Such rules are necessary to make the system effective and enforce the policy against secret liens.

A similar policy underlay the Canadian reforms.

But a policy against "secret liens" that is protective of general creditors is only appropriate if it is seriously believed that without it general creditors in making their decisions to grant credit will be deceived. Now two committees appointed to review the law of bankruptcy, one by the President of the Board of Trade in the United Kingdom, which reported in 1955 (Cmnd 221, para 110), and one by the Attorney-General of the Commonwealth of Australia, which reported in 1962, both recommended the abolition of the reputed ownership provision in the bankruptcy statute on the grounds of its obsolescence, there being (in the words of the Australian committee) "little, if any, danger nowadays of a creditor being induced to give credit on the assumption that goods in the debtor's possession are his own property" (para 153). Those responsible for the review of New Zealand's bankruptcy law agreed with this view, and the reputed ownership provision (s 61(c), Bankruptcy Act 1908) was not re-enacted in our Insolvency Act of 1967. There has never been any comparable provision in the law relating to the distribution of the assets of insolvent companies. It is not logical on the one hand to abolish for the reasons stated the reputed ownership provision of the bankruptcy law and on the other to preserve in chattels securities legislation a provision of which the very premise was rejected in settling that insolvency law.

The argument, then, is this. In the case of individuals credit is not today granted on the basis of appearances, so that consistently with the repeal of the apparent ownership provision by the Insolvency Act 1967 there is no logical basis for avoiding unregistered instruments against assignees in bankruptcy or execution creditors as distinct from specific disponees such as purchasers and subsequent encumbrancers. In the case of companies there never has been an apparent ownership provision and because disclosure is best regulated systematically by such provisions as the Financial Reporting Act 1993, it should not be a function of the proposed Personal Property Securities Act to publicise the company's financial position. There is no justification, therefore, for providing that an unregistered security may not be enforced against liquidators or execution creditors.

It may be noted that the effect of the Motor Vehicles Securities Act 1989 is the same as that proposed for the Personal Property Securities Act.

There is in addition the more elegant point made by Peter Watts commenting on my paper at the symposium at which it was presented namely, that:

> ... a legal regime which requires only security interests to be registered is one which operates so partially as not to give a great deal of comfort to general creditors. It might also be perceived as punitive on the one class of property interest which has been singled out. Furthermore, it is doubtful whether many general creditors, even those who are relying on the fact of the debtor's possession of chattels, would search a register.

I should note that I have been unable to persuade Professor Goode to the view advanced in this note. He has written:

> The effect of avoidance is thus to give unsecured creditors who did not act in reliance on the want of registration an apparently unjustified windfall addition to the assets available for distribution.
>
> Yet there are sound policy reasons for the avoidance of unregistered securities. In the first place, the avoidance rule reflects the law's dislike of the secret security interest, which leaves the debtor's property apparently unencumbered and at common law was considered a fraud on the general creditors. Secondly, the registration provisions help to curb the fabrication or antedating of security agreements on the eve of winding-up. Thirdly, though unsecured creditors have no existing interest in the company's assets outside winding up, and thus no immediate locus standi to complain of want of registration, they have an inchoate interest, in that upon winding up the whole of the company's property, so far as not utilised in discharging the expenses of the winding up and the payment of preferential claims, becomes available for the general body of creditors, so that their rights become converted from purely personal rights into rights more closely analogous to that of beneficiaries under an active trust. Fourthly, there may well be unsecured creditors who were misled by the want of registration into extending credit which they would not otherwise have granted. But it would be both expensive and impracticable to expect the liquidator (or administrator) to investigate each unsecured creditor's claim to see whether he did or did not act on the assumption that the unregistered charge did not exist. So a broad brush approach which in effect assumes detriment to unsecured creditors at large is justified. Finally, the registration provisions serve a general public notice function as well as being a perfection requirement, and the avoidance provision can be seen as an inducement, and a powerful inducement, to comply with the requirements of the law, reinforcing criminal sanctions for non-compliance. However, these policy considerations have been somewhat undermined by decisions holding (correctly in terms of legal analysis) that to the extent that the security has already been enforced or paid off prior to the winding-up or other invalidating event its avoidance has no effect. (R M Goode, *Principles of Corporate Insolvency Law* (2nd ed 1997 420-421).

One does not lightly disagree with Professor Goode but none of his reasons seems particularly plausible

The reasons for the dislike of the secret security interest were solely the possibility of obtaining credit from creditors misled by borrowed plumes, which as already discussed is not how business is done in 1998.

There is no reason to believe that there is genuinely a problem with fabricating or ante-dating security agreements.

The third argument does not advance the matter; it suggests a logical consequence of the liquidator or administrator being able to defeat the unperfected interest but is not itself an argument for the liquidator or administrator having that right.

The fourth point merely repeats the discredited reliance on apparent ownership to extend credit argument.

The final point as to public notice has already been discussed. Under the proposed statute there is no duty to register or criminal sanctions for non-compliance any more than under the Chattels Transfer Act 1924. Why should there be? There is no time limit for registering; the only risk run by delaying is losing one's place in the queue.

REGULATING ENFORCEMENT

For a long time the odd (though readily explicable historically) state of New Zealand law was that it provided for debtors where title was reserved under hire purchase agreements protections that were not available where the security

was an instrument by way of security performing an identical economic function. When to avoid the new duties imposed by the Hire Purchase Act 1971 there was an increase in the use of instruments by way of security, the response of the legislature was in 1974 to amend the definition of hire-purchase agreement in that Act to include instruments in favour of or procured by dealers. It was a conceptually curious but practically effective solution.

The bringing to an end of this anomalous situation of having different protections for transactions that were really doing the same job was a principle purpose of the Credit (Repossession) Act 1997. (A purist would cavil at the prefix Re.) It is a statute that it should have been possible to welcome unreservedly. But unhappily the measure has been botched in important respects. It would be tedious to go into technical detail. There are useful discussions by Mr Barry Allan and Professor McLauchlan in the August 1998 number of NZBLQ. But attention should be drawn to the following matters which seem to the writer particularly outrageous.

The great achievement of the Hire-Purchase Agreements Act 1939 was to bestow on hire-purchasers something roughly equivalent to a mortgagor's equity of redemption. If after repossession the proceeds of sale left something over once the original obligation (subject to any interest adjustment) was satisfied that surplus went to the purchaser. This meant an end to the situation of a purchaser defaulting and having goods snatched from him when they were paid for nearly in full and so losing both the whole of the money already paid and the goods. The 1939 measure was strengthened by the Hire Purchase Act 1971 which improved the machinery and also required in most cases notice before repossession.

The three most important respects in which the 1997 statute has weakened the debtor's position are these.

- Under s 34 the debtor must now commence proceedings to recover any refund within six months of receiving the statement following sale of the goods. Why (particularly considering that debtors are likely to be commercially unsophisticated) should the creditor be allowed to pocket the money after so short an interval? The departmental justification was the administrative costs of keeping numerous small balances identifiable. One's heart bleeds of course for those faced with these costs, but surely an honest trader would simply send a cheque with the post-sale statement. This new time limitation seems an odd way of protecting the disadvantaged.
- Secondly, s 42 permits contracting out where the goods are used for the purpose of a business unless the goods were being acquired under a hire-purchase agreement. It is difficult to see why there should be different rules for hire-purchase agreements and for instruments by way of security in relation to contracting out, particularly remembering that as mentioned above, the relevant definition of hire purchase agreement includes some instruments by way of security. We may expect in the case of business goods instruments by way of security to replace hire purchase agreements and contracting out to become a normal part of the fine print. It is even less clear why contracting out should be forbidden where the chattel is an expensive motor car but allowed in the case of a farm bike or a corner dairy's cash register. The small trader does not cease to need protection simply because a chattel is used for commercial purposes.
- Thirdly the Hire Purchase Act 1971 provided by s 26(2) that a purchaser could apply to a District Court for relief even though there was a contractual entitlement to repossess. What was envisaged was a procedure under which a drought-stricken farmer for example could seek an extension of time on appropriate terms. This provision has been replaced by s 12 of the 1997 Act. Some clever person has changed s 26(2) to confine the right to claim relief to the situation where the creditor has acted in contravention of the Act, thereby completely defeating the purpose of the original provision, and substituting a remedy that would probably exist without the section.

So what is to be done? The obvious solution is to await the passage of the proposed personal property securities legislation and then to knock the Credit (Repossession) Act 1997 into sensible shape using the personal property securities definitions.

What should not be done is to include in the personal property securities legislation provisions regulating the enforcement by security holders of their powers.

The purpose of the Personal Property Securities legislation is to provide a system to resolve the disputes as to title that can arise when Party A has possession of goods, Party B has a security interest in the goods and Party C claims the goods as buyer or security holder in priority to B.

The benefit of the scheme to B is that he can have confidence that the priority of his security is preserved. The benefit of the scheme to C is that he is able by searching before altering his position to be confident that he is getting the title he bargained for. The benefit of the scheme to A is that the confidence so imparted to B and C helps A in selling his personal property or using it as a security.

The statute then is intended to provide a machinery regulating priorities. It has no more to do with the fairness of the arrangements between debtor and secured party than has the Land Transfer Act 1952 with the fairness of the terms of mortgages registered pursuant to its provisions or of the exercise by mortgagees of their powers.

This is not to deny that there can be benefits in the inclusion of standard terms in machinery statutes, to avoid their having to be repeated in every instrument. Familiar examples are the Chattels Transfer Act 1924 Third, Fourth and Fifth Schedules and the Land Transfer Act 1952, Third, Fourth and Seventh Schedules. In the case of the personal property securities legislation, however, it is doubtful whether it is possible to devise a single set of rules to regulate all the different types of affected transactions. There is, in any event, no point in drawing such provisions in some sort of crusading consumer protection spirit. Their whole purpose is destroyed if they lean so far in favour of the debtor that they have in every document to be amended.

It is for these sorts of reasons that the Law Commission in its 1989 report *A Personal Property Securities Act for New Zealand* (NZLC R8 p 12, 162 – 164) rejected North American examples and carefully excluded any regulation of default powers from its draft Bill. Apart from the sheer inappropriateness of cluttering the measure with such provisions, it would be sad to see the enactment of these elegant reforms further held up while conflicting interests bicker over consumer protection issues.

It will be important to ensure that in the New Zealand statute such matters are left outside the personal property securities legislation and to the extent that they need legislative attention at all confined to a revamped Credit (Repossession) Act. ❑

THE NEW ARBITRATION ACT

David A R Williams QC

reviews some cases and problems and makes some practical suggestions

It is a year since the Arbitration Act 1996 came into force. On its first anniversary it is appropriate to highlight some problem areas of the new Act, discuss some of the early decisions, and suggest some practical steps which may help to ensure that arbitration is an effective and efficient mode of dispute resolution. The principle of party autonomy enshrined in the Act opens up many procedural choices. For a discussion of these choices see Master Kennedy-Grant and D S Firth *The Challenge of Choice: Arbitration Agreements Revisited* (Auckland District Law Society, 1998). It is most important that practitioners appreciate that arbitration will not be efficient and cost-effective if it is undertaken in a way which simply replicates Court procedures. In particular, costs must be reduced through shortening the length of oral hearings and, in line with developing international arbitration practice, emphasising the importance of documentary evidence while at the same time simplifying otherwise expensive discovery procedures.

THE KEY CONCEPTS

By now the main features of the new law are fairly well-known. It has as its key themes party autonomy, reduced judicial scrutiny, and increased powers for the arbitral tribunal. In the first Court of Appeal pronouncement on the new Act Keith J remarked that the Act takes "further the recent tendency in cases and legislation in various jurisdictions to narrow the scope of Court review and give greater autonomy to the arbitration": *T H Barnes & Co Ltd v The Minister of Inland Revenue* [1998] 2 NZLR 463, 465. The Act is based on the Model Law on International Commercial Arbitration adopted by the United Nations Commission on International Trade Law (UNCITRAL) in June 1985. However, as suggested in the Law Commission's Report, it adds to or departs from the Model Law in a number of important respects.

For more detailed discussion the reader is referred to D A R Williams and F J Thorp, *The Arbitration Act*, (Wellington: New Zealand Law Society, 1997); A A P Willy, *Arbitration in New Zealand*, (Wellington: Butterworths, 1997); D A R Williams, *Arbitration and Dispute Resolution* [1998] NZ Law Review 1; Master Kennedy-Grant and D S Firth, *The Challenge of Choice: Arbitration Agreements Revisited* (Auckland District Law Society, 1998).

As to its structure, the heart of the Act is to be found in s 6. This effectively divides arbitration into domestic arbitrations (ie those held in New Zealand between New Zealand parties) and international arbitrations (ie those where the parties to an arbitration agreement have at the time of the conclusion of that agreement their places of business in different countries or where certain other international elements are present). In the case of both domestic and international arbitrations "the rules applying to arbitration generally" and contained in the First Schedule to the Act apply. These correspond for the most part to the provisions of the Model Law. The Second Schedule contains additional optional rules. The Second Schedule applies to an international arbitration *only if the parties so agree*. However, the provisions of the Second Schedule and its additional optional rules apply to domestic arbitrations *unless the parties agree otherwise*. This has immense significance for legal practitioners who must carefully consider whether in a domestic arbitration they wish to specifically exclude some of the optional rules which will otherwise apply pursuant to the Second Schedule.

TRANSITIONAL PROVISIONS

The profession does not seem to have done a good job in understanding the transitional provisions contained in s 19. The general rule, as set out in s 19(1)(a) is that the Act applies "to every arbitration agreement, whether made before or after the commencement of this Act, and to every arbitration under such an agreement". This provision was tested in *Hitex Plastering Ltd v Charles Speedy Developments Ltd*, High Court Auckland, M1501/97, 21 October 1997, Morris J. The defendant had failed to appoint an arbitrator, as it was required to do by the arbitration agreement. The plaintiff had brought an application for the Court to appoint an arbitrator. The contract provided for arbitration under the Arbitration Act 1908. It was submitted that as this had been repealed there was therefore no provision for arbitration. This argument was summarily disposed of by Morris J who quite rightly pointed to s 19(1)(b) of the Act where it is stated "[a] reference in an arbitration agreement to the Arbitration Act 1908 ... shall be construed as a reference to this Act ...". It appears that neither counsel seemed to realise that, while it was necessary for an application to be made to the Court in such circumstances under the 1908 Act, this is not necessary under the new Act. Hitex, under cl 1 of the Second Schedule (this being a domestic arbitration where the Second Schedule had not been excluded) had the ability to issue a notice requiring Charles Speedy to remedy its default. Hitex could then have proposed that otherwise its named arbitrator should be appointed to the office of arbitrator. Clause 1 has been designed to enable parties to commence arbitrations, without the need to resort to the Courts, if problems arise in the appointment of the arbitral tribunal.

There are, however, two exceptions to the general coverage rule of s 19(1)(a). First, where an arbitration is commenced before 1 July 1997, s 19(2) provides that "the law

governing the arbitration agreement and the arbitration shall be the law which would have applied if this Act had not been passed". In view of the passage of time since 1 July 1997 this provision is increasingly unlikely to apply.

The second exception, contained in s 19(3), is more controversial. That subsection provides:

> (3) Where an arbitration agreement, which is made before the commencement of this Act, provides for the appointment of two arbitrators, and arbitral proceedings are commenced after the commencement of this Act, –
>
> (a) Unless a contrary intention is expressed in the arbitration agreement, the two arbitrators shall, immediately after they are appointed, appoint an umpire; and
>
> (b) The law governing the arbitration agreement and the arbitration is the law that would have applied if this Act had not been passed.

The practical implications of this latter subsection are quite significant. Contracts made before 1 July 1997 containing arbitration clauses providing for the appointment of two arbitrators are commonplace. Many of those contracts are likely to remain in force for years to come – for example, contracts of supply, franchise agreements, leases, partnership agreements, joint ventures. Arbitrations commenced under agreements of this kind, whether one, two or 20 years hence, will continue to be governed by the existing law – the 1908 and 1938 Acts and associated common law rules – rather than the new Act, unless the parties agree to recast their arbitration agreement. Arbitrators will therefore need to retain, or develop, as the case may be, a familiarity with the old law for many years to come.

In so far as arbitral awards (as opposed to arbitration agreements or arbitral proceedings) are concerned, s 19(5) provides that the Act applies to *every* arbitral award "whether made before or after the commencement of this Act".

The profession has not done too well under this provision either. However, in fairness, as Cartwright J observed in *Helleur v Helleur* [1998] 2 NZLR 205 at 211 (1997) 11 PRNZ 662, 667, there is some lack of clarity in its application. In the Court of Appeal in *T H Barnes* it transpired that the parties had conducted a High Court review of an arbitral award under the 1908 Act, without understanding that s 19(5) made the new Act applicable. In the High Court the minister had successfully applied for an order setting aside the award for error of law on the face of the award. The Act had come into force after the making of the award, and after the bringing of the High Court challenge, but before the hearing in the High Court and its judgment. It was accepted by counsel in the Court of Appeal that the award would not have been set aside under the new Act. Accordingly, the question was whether the new Act applied to the award even though it was given in October 1995 and the High Court proceedings were begun in October 1996. The judgment of the Court was delivered by Keith J who noted that the usual presumption that legislation has only prospective effect is not an invariable rule. He continued (supra at 466):

> The transitional provisions included in s 19 of the Act make it clear that the new provisions are to be applicable not simply to arbitration agreements, proceedings and awards of the future. It has retrospective effect. So far as awards are concerned, subs (5) provides:
>
> > This Act applies to every arbitral award, whether made before or after the commencement of this Act.
>
> ...
>
> Subsection (5) is expressly comprehensive applying to arbitral awards made earlier, as in the present case. By contrast to subs (1) it is not subject to any exception. Section 19 distinguishes between arbitration agreements, arbitral processes and arbitrations under arbitration agreements, on the one side, and arbitral awards, on the other. It is the latter which is in issue here ... and so far as awards are concerned, subs (5) is in categorical terms. The new law applies to any challenge to that award and, as noted earlier, no basis was suggested for a challenge under that new law. It follows that the appeal has to be allowed.

The respondent raised the unfairness of it being deprived of the wider basis for review available under the old law. The Court did not question that the major justification for the principle against the retrospective application of new law is that it is unfair to deprive parties of rights or expectations established under earlier law. However, the Court felt the particular subject matter and context of this statute affected the application of this principle. Reference was made to the Court's increasing reluctance to intervene in parties' arbitration agreements, and the Law Commission's conclusion it was proper to provide for the early application of the Act and the avoidance of a lengthy transitional period.

Section 19(5) was also the cause of some confusion in *R H Page Ltd v Hitex Plastering Ltd*, High Court Auckland, CP 428/97, 22 December 1997, Paterson J; 2 April 1998, Paterson J; and 19 June 1998, Salmon J. The situation here was that an application had been filed to set aside an award made on 28 July 1997 (ie after the commencement of the new Act), on the grounds of error of law on the face of the award. Paterson J found the arbitrator had erred in law but dismissed the application because it related to a specific legal issue which had been referred to the arbitrator, and which consequently was not reviewable. As the arbitration had commenced before 1 July 1997, both counsel took the view that the Arbitration Act 1996 did not apply and the matter was governed by the Arbitration Act 1908 and the common law principles. In the first decision in these proceedings dated 22 December 1997, Paterson J noted the existence of s 19(5) and stated at p 14:

> It is noted that there are divergent views on the application of this sub-section: (see para AR 19.06 of *Brookers Arbitration Law & Practice*). It may well be that the provisions of para 5 of the Second Schedule of the Arbitration Act 1996 apply in these cases. This matter has not been argued before me and consequently, I do not intend to make a determination on it. If the 1996 Act does apply I would have come to the same conclusion as I have come to above as I do not see the procedural provisions in para 5 of the Second Schedule affect the substantive provisions upon which I have come to my conclusion.

Subsequently the parties realised the 1996 Act did apply, and the party challenging the award applied for leave to appeal from the judgment of the High Court. This was refused by Paterson J in a decision dated 2 April 1998 on the grounds the Court did not have jurisdiction to grant leave in accordance with the terms of the application. An application was then made for leave to appeal from the arbitral award pursuant to cl (5)(1)(c) of the Second Schedule to the 1996

Act. Salmon J declined to grant leave in a decision dated 19 June 1998. This decision will be considered later in this article under the topic of appeals on questions of law.

Another difficult question is whether the provisions for setting aside arbitral awards under the 1996 Act apply to the conduct of arbitrations under the 1908 Act or whether they apply only to enforcement of the arbitral award. This question was considered by Cartwright J in *Helleur v Helleur*. The case concerned an award issued in November 1996 in respect of which an application to set aside was lodged before 1 July 1997. The grounds on which the plaintiffs submitted the award should be set aside were all concerned with the conduct of the arbitral proceeding by the arbitrator. At 209 of her decision Cartwright J observed the plaintiffs' rights to seek the Court's intervention "would be sharply limited by the provisions of [Articles] 34(2)(b)(ii) and 6(b)" if the 1996 Act applied. Cartwright J referred to, and adopted, the Law Commission's statement at para 275 NZLC R20, that:

> [Section 19(5)] makes it clear that the new Act will apply to the recognition and enforcement of an award, even when the arbitral proceedings which led to the award had been commenced before the entry into force of the draft Act and so were governed by the pre-existing law under [s 19(2)].

Her Honour rightly observed at 210-211 that the Law Commission's report was part of the legislative history to which resort might be had to resolve ambiguities in the Act. Section 3 of the Act explicitly provides that the legislative history of the Model Law may be referred to in interpreting the Act. This material may be found in NZLC R20 or Hotlzmann and Neuhaus, *A Guide to the UNCITRAL Model Law on International Commercial Arbitration*, 2nd ed (Boston: Kluwer, 1994).

Relying on this interpretation, and on the "inherent unfairness [of insisting] on applying the 1996 Act to a completed arbitration in respect of which proceedings had been commenced before the Act came into force", Cartwright J held at 211 that "[w]hile the enforcement of the award may logically be conducted under the 1996 Act, the arbitral proceedings themselves should be governed by the law applicable at the time they were conducted and completed". Cartwright J thus read down subs 5, restricting its application to the enforcement of awards and not to the issue of setting aside awards for misconduct during the arbitral procedure. Her Honour stated at 209:

> The reason for distinguishing between proceedings and awards is deliberate. The proceedings are governed by the law which applies while they are under way. Parties require the certainty of applicable law and legislation while they are undergoing arbitration or negotiating to settle.

Although the judgment has been criticised (D A R Williams, *Arbitration and Dispute Resolution* [1998] NZ Law Review 1 at 8; Master Kennedy-Grant and D S Firth, *The Challenge of Choice: Arbitration Agreements Revisited* (ADLS 1998) pp 14-16), it derives some support from *T H Barnes*. Keith J, who delivered the judgment of the Court, identified a distinction in s 19 between arbitration agreements, arbitral processes and arbitrations under arbitration agreements, on the one side, and arbitral awards, on the other. At p 466 Keith J observed that any challenge relating to the validity of the arbitration agreement or the process followed in the course of the arbitration would, in terms of s 19(2), be in accordance with the law which would have been applicable had the new Act not been passed, ie the 1908 and 1938 Acts and associated common law rules. Even though *T H Barnes v Minister of Inland Revenue* was an application to set aside an award, the distinction drawn by Keith J should, however, be equally applicable if a party is seeking to defend an enforcement application.

This distinction was affirmed by a differently constituted Court of Appeal in *City House Properties Ltd v J C & C P Fergusson Ltd*, CA 209/97, 29 June 1998. This case concerned an appeal from a decision of the High Court remitting an arbitration award to the arbitrator for reconsideration on the ground material evidence had been discovered since the hearing of the arbitration. The arbitration and the award had both occurred prior to the new Act coming into force. Thomas J, delivering the judgment of the Court, stated at p 6:

> Because the proceedings relate to the arbitration and, in particular, to the procedure followed, rather than to the award itself, the Arbitration Act 1908 continues to be applicable, notwithstanding the fact that it has been replaced by the Arbitration Act 1996 in the meantime. (Compare s 19(2) of the 1996 Act with s 19(5).) The grounds for review under the new Act are in general narrower and review may well not have been possible in the current case had the arbitration commenced after the new Act came into force.

Both *Helleur v Helleur* and *T H Barnes* were cases in which review proceedings had already been commenced in the High Court *before* the 1996 Act came into force. Notwithstanding this, in *T H Barnes* the Court of Appeal held the new Act applied when the award itself was challenged.

A further issue, which has yet to be raised in the Courts, relates to awards arising out of arbitration proceedings conducted under the old law, by virtue of s 19(3), because the arbitration agreement provided for two arbitrators and an umpire. Section 19(3) only refers to the "arbitration agreement" and the "arbitration" being governed by the old law. It does not refer to the "award". For this reason some commentators conclude such an award will become subject to the law under the 1996 Act: P Green and B Hunt, *Brooker's Arbitration Law & Practice* (Wellington; Brookers, 1993) para AR19.05. The decision of the Court of Appeal in *Barnes* seems to support such a conclusion.

UNRESOLVED MATTERS

While the Arbitration Act 1996 contains a valuable modernisation of our country's arbitration laws, like any new legislation, it contains a few unresolved issues. The transitional provisions have already been referred to. In addition there are several other points which are unclear or difficult.

Arbitration agreements in contracts with consumers

An important transitional point should be noted in relation to s 11 of the new Act. Section 11 sets out certain criteria which must be fulfilled, in respect of arbitration agreements contained in contracts which one party has entered into as a consumer. The effect of non-compliance with s 11 is that the arbitration agreement will not be enforceable against the consumer. As there is no monetary limit referred to in s 11, it therefore affects all businesses whose standard form contracts with consumers contain arbitration clauses.

Practitioners need to know that s 11 will apply whether or not the arbitration agreement was entered into before

1 July 1997 (unless, of course, the arbitration agreement provides for two arbitrators and therefore falls within s 19(3)). Thus an arbitration agreement made with a consumer and which would have been enforceable under the existing law, will not be able to be enforced against the consumer after 1 July 1997 unless the consumer executes a separate written agreement which complies with s 11(1) or either waives his or her right to object pursuant to Art 4.

Service by facsimile?

Article 3 sets out the rules relating to receipt of written communications. It provides that "[a]ny written communication is deemed to have been received if it is delivered to the addressee personally or if it is delivered at the addressee's place of business, habitual residence, or mailing address". No mention is made in Art 3 of service by facsimile. The issue is whether a facsimile transmission arriving on the addressee's facsimile machine constitutes delivery at the addressee's place of business. It is submitted the answer is not clear and if it is intended that communications by facsimile should be allowed, RR 192 and 206A of the High Court Rules should be written into the arbitration agreement.

Appointment of arbitrators under cl 1

Clause 1 of the Second Schedule provides a procedure for appointment of arbitrators which is deemed to have been agreed upon by the parties under Art 11. As it is in the Second Schedule, unless an express agreement to the contrary is reached, parties to a domestic arbitration will be taken as having agreed to the procedure set out therein. The default provisions for appointment of the arbitrator are contained in subcls (4) and (5).

Of these provisions, cl 1(4)(b) is deserving of mention as it may give rise to practical problems. It suggests that an inability by the parties or the arbitrators to reach agreement on the person or persons to be appointed as arbitrator, amounts to a default; and that any party may then issue a written notice specifying the details of the default (ie failure to agree) and propose that, if that default is not remedied within a period of not less than seven days, that a person named in the written notice shall be appointed to such vacant office of arbitrator (for example, sole arbitrator) as is specified.

Such an interpretation would in one sense seem to encourage the creation of a disagreement with a view to being the first to issue a default notice, safe in the knowledge that in seven days, their named arbitrator will fill the vacant position. It is questionable whether any right of appeal exists in respect of such an appointment. At para 418, the Law Commission noted that it had not recommended a power for the Court to set aside a default appointment. Moreover, art 11(4) precludes the making of any request to the High Court if the agreement on the appointment procedure provides other means for securing the appointment.

Liability of arbitrators

The issue of the liability of arbitrators is addressed in s 13 of the new Act. Section 13 provides "[a]n arbitrator is not liable for negligence in respect of anything done or omitted to be done in the capacity of arbitrator". Whilst s 13 removes any liability for negligence in respect of anything done or omitted to be done in the capacity of arbitrator, it is clear that the section is not intended to provide arbitrators with absolute protection from suit. In particular it will not protect a fraudulent arbitrator, and its protection does not extend to all kinds of civil claims, eg defamation. Furthermore, it is unclear whether an arbitrator found, in good faith, to have been acting in excess of jurisdiction, is protected. This issue is dealt with in a more comprehensive form in the Arbitration Act 1996 (UK), s 29(1) of which provides:

> An arbitrator is not liable for anything done or omitted in the discharge or purported discharge of his functions as arbitrator unless the act or omission is shown to have been in bad faith.

In circumstances where s 13 provides limited protection only, it may be sensible for arbitrators to expressly exclude by contract liability for all civil claims. However, attempts to include such provisions can create sensitivities with the parties.

Confidentiality

Section 14 creates a general rule of confidentiality but allows the parties to agree otherwise. It overcomes the decision of the High Court of Australia in *Esso Australia Resources Ltd v Plowman* (1995) 128 ALR 391 which held, contrary to widespread understandings in most jurisdictions, that there is no firm legal basis to support the confidentiality of information generated in a commercial arbitration, as distinct from the privacy of the arbitral hearing. Section 14 does not prevent disclosure of information to a professional or other adviser of any of the parties, nor any publication, disclosure or communication contemplated by the new Act. It has been observed that the Official Information Act 1982 would probably override this provision: See Arbitration Bill: Third Report of the Minister of Justice and the Department for Courts, 16 July 1996, p 5. The result is that, unless otherwise agreed, material produced for, or generated by, an arbitration cannot be disclosed by the parties to third parties or used for purposes unconnected with the arbitration. It should be observed, the stringency of this provision may lead to problems if the parties do not agree to exceptions. Parties may have pre-existing contractual obligations to provide information relating to the award such as those contained under the Stock Exchange requirements.

STAY OF COURT PROCEEDINGS

Article 8 of the First Schedule imposes a mandatory obligation on the Court to stay Court proceedings if a valid agreement exists for arbitration, subject to specifically defined grounds on which the Court must refuse to stay the Court proceedings. Article 8 is one of the provisions of the Act reflecting emphasis on increased party autonomy and reduced judicial intervention. One ground on which the Court must refuse to stay Court proceedings is "that there is not in fact any dispute between the parties with regard to the matters agreed to be referred". This exception was not present in either the 1908 Arbitration Act, the 1982 Arbitration (Foreign Awards and Agreements) Act 1982 or the model law. The Law Commission indicated at para 309 of NZLC R20 it was included so "the efficiency of the summary judgment procedure as it has developed under the High Court Rules should not be lost by reason of any implication that a dispute where there is no defence must be arbitrated under an arbitration agreement".

This exception is also not present in the Arbitration Act 1996 (UK). In *Halki Shipping Corp v Sopex Oils Ltd* [1997] 3 All ER 833 it was held that under s 9(4) of the

continued on p 392

CONTINGENCY FEES: RISKIER THAN THEY SEEM

Duncan Webb, Victoria University of Wellington,

asks whether an increasingly common practice is within the law

Contingency fees are frequently used in one form or another to fund litigation in New Zealand. Any arrangement whereby the existence or amount of the fee is dependant on the outcome of litigation can be termed a contingent fee, although those where the proposed fee is inflated to allow for the risk of non-payment are more usual. There are strong arguments for making such arrangements legal, at least in some situations (see K Tokeley "Taking a Chance: A Proposal for Contingency Fees" (1998) 28 VUWLR 13). I do not propose to traverse those arguments. Rather, this article is concerned with the fact that current legal practice seems to ignore the law as it stands, and accordingly many practitioners are exposing themselves to considerable legal and professional risks.

While members of the profession and the Courts have always regarded the rules propounded by the Law Society as a reliable indicator of acceptable professional standards and conduct, it is not the arbiter. Furthermore, it is not open to the Law Society to make permissible a practice currently prohibited by law, by a change in the Rules of Professional Conduct for Barristers and Solicitors.

The starting place when considering what kind of fee arrangement to enter into with a client must be based on the law as it stands. This paper argues that an arrangement under which a lawyer obtains an increased fee for a successful prosecution of litigation is illegal. A contingency fee in New Zealand breaches two rules of law. Firstly it is champertous, a form of the old tort of maintenance. Secondly it is a contract which is illegal as against public policy and therefore void.

THE NEW ZEALAND POSITION

The starting position for a lawyer in New Zealand considering entering into a contingency fee arrangement must be that it is both champertous and illegal as contrary to public policy. The New Zealand Law Society has declined to give direction to its members by stating that its R 3.01 (which deals with fee setting), "is drafted in terms which contemplate the possibility of charging a contingency fee" but drawing attention to the fact that the legality of such fees is questionable. Similarly in the recent "Report of the Auckland District Law Society Working Group on Contingency Fees" concluded that under the current law "with certain exceptions, contingency fees in relation to litigation are likely to be held unlawful and/or unenforceable" (p 2). In fact the law on contingency fees in New Zealand is more inconvenient than questionable. The leading authority from the Court of Appeal of *Mills v Rogers* (1899)18 NZLR 291 may be old, but it is not equivocal, as some have suggested, and it has not been overruled.

That case concerned an arrangement under which actions in defamation were taken against certain newspapers. It had been agreed in respect of fees that "the plaintiff should not be called upon to pay any expenses whatever, but should receive from the [solicitor] one third of the net amount recovered after deducting certain expenses" (p 293). The dispute in hand was an action by the litigant against his solicitors who had been successful in one action and unsuccessful in another. The question was whether the terms of the agreement meant that certain costs awarded against the plaintiff in the unsuccessful action were to be paid from the damages awarded in the other action (and reducing the solicitor's fee) or not.

The arrangement was clearly a contingency fee, albeit one with an astronomical proportion of the proceeds (66 per cent) going to the solicitor. On this basis the solicitors pleaded "their own rascality" (p 298), namely that the arrangement was champertous, and therefore void and unenforceable against them. Denniston J, in the High Court, took an unequivocal view of this arrangement:

> It is maintenance because it is an agreement to supply legal assistance and money by persons not interested legally or morally in the litigation; it is champerty because it is in effect an agreement to be repaid in the event of success by a part of the subject-matter of the litigation. It is therefore void ... (p 296)

The Court of Appeal unanimously affirmed this view. In Williams J's terms:

> It was ... a partnership agreement, into which one partner contributed to the common stock certain rights of action for libel, and the others, who had no moral or legal interest in the litigation, their legal skill. The proceeds were to be divided, and the partner who contributed the rights of action was to be indemnified against loss. An arrangement more calculated to foster and encourage improper litigation and unscrupulous professional conduct can hardly be conceived. The agreement being thus illegal, it is incapable of being enforced in an action. (p 309 – 310)

The existence of the rule against champerty in New Zealand was also affirmed in *Heni Materoa v Finn* (1902) 20 NZLR 67 where it was held that an arrangement which effectively transferred the proceeds of litigation to a solicitor was a fraud on the client and void. The High Court again applied the rules of maintenance and champerty in *Sievwright v Ward* [1935] NZLR 43 in finding an arrangement to pay normal fees only from the proceeds of the action not to be champertous. The latter case is of particular interest as it

seems to follow very closely the reasoning in the recent English Court of Appeal decision of *Thai Trading v Taylor* [1998] 3 All ER 65 in finding that an arrangement that normal fees and disbursements be paid out of the proceeds of litigation is not champertous.

Some commentators have claimed recent judicial acceptance of contingency fee arrangements in New Zealand by virtue of their unobjectionable mention by the Court in several judgments. Those commentators rely on certain cases where Masters of the High Court have held that the existence of a contingency fee arrangement will be relevant to whether an order of security for costs will be granted: *Nikau Holdings Ltd v Bank of New Zealand* (1992) 5 PRNZ 430, (1992) 6 NZCLC 67,939; *Gosper v Re Licensing (NZ) Ltd* (1997) 11 PRNZ 34; *Vincent Aviation Ltd v Director of Civil Aviation* HC, Wellington CP 779-92 13 May 1994 Master Thompson.

Those cases are in fact of little assistance. None of the Masters who decided those cases were required to turn their mind to the question of champerty, or the legality of the fee arrangements. This is apparent in the cases themselves which deal with the fee arrangement only in terms of its relevance to security for costs. In any event none of those cases demonstrate that there was any increase of the fee due to the contingency arrangement – and therefore champerty. Those cases do not alter the old law that champertous arrangements are a tort against the defendant and an illegal contract.

ENGLISH REFINEMENTS

Up until the passing of the Criminal Law Act 1967 which abolished the torts (and crimes) of maintenance and champerty the English Courts frequently recognised the contractual and tortious implications of champertous arrangements. Since then English cases have been concerned only with the contractual effects of such arrangements which has been left unchanged by the law reform. In *Thai Trading v Taylor* the Court of Appeal was called upon to refine the concept of what kind of arrangements are champertous and therefore illegal.

The case concerned a no-win no-fee arrangement. It was, however, unusual in a number of respects. First, the fee payable on success was not inflated to take account of the risk of no fee – only the normal fee was payable in the event of success. Second (and the reason for the generous arrangement) the litigant was the wife and employee of the solicitor who acted for her in the litigation. The Court dealt with the question of whether the arrangement was illegal for breach of public policy and therefore void. The question arose in the context of an appeal against an award of costs. The losing defendant against whom costs had been awarded argued that the award was inappropriate because the successful plaintiff had not incurred any legal obligation to pay for costs due to the illegality of the fee arrangement. Thus on the authority *Gundry v Sainsbury* [1910] 1 KB 645 it was not open to the Court to order that the defendant pay costs as they are by way of indemnity only.

The Court of Appeal took the view that any arrangement which would have been champertous under the old law was contrary to public policy. Indeed the law reform which abolished the crime and tort of champerty expressly left unaltered the fact that such arrangements fall into that category of contract which are considered to be contrary to public policy. It is of particular note that this finding was made notwithstanding that specific provision has been made to accommodate certain contingency fee arrangements in the Courts and Legal Services Act 1990 and regulations made under that Act. The Court took the view that the liberalisation of the law demonstrated a need to determine what kind of fees were acceptable, rather than a wholesale acceptance of all contingency fee arrangements.

Millet LJ traversed some of the cases on maintenance and champerty and cited from *In Re Trepca Mines (No 2)* [1962] 3 All ER 351, where Lord Denning stated that such arrangements mean the champertous advocate "might be tempted for his own personal gain, to inflate damages, to suppress evidence, or even to suborn witnesses". The intolerance of the English Courts to contingency fees, unless authorised by statute, has continued unabated. See *Wallersteiner v Moir (No 2)* [1975] 1 All ER 849; *Trendtex Trading Corporation v Credit Suisse* [1981] 3 All ER 520 (46).

In *Thai Trading* Millet LJ took the opportunity to review these cases and define more clearly those cases which were champertous and those which were not. In particular he found that an arrangement of the kind in that case where there was no fee in the event of a loss, but the normal fee in the event of a win was found not to be champertous. It was noted that it is always open to a lawyer to waive the payment of fees. In the present case the arrangement amounted to no more than a conditional waiving of fees. In reaching this decision His Honour overruled the decision in *Aratra Potato Co Ltd v Taylor Joynson Garret* [1995] 4 All ER 695 where a reduced fee was agreed in the event of a loss was found to be against public policy and unenforceable. The case arguably went no further than Ostler J in *Sievwright v Ward.* There an arrangement where a lawyer agreed to take his or her reasonable fees and disbursements from the proceeds of the litigation where the litigant was impecunious, was considered "not only lawful, but consistent with the highest professional honour" (p 48).

This recognises that in considering what kinds of fees are champertous and illegal it is appropriate to look beyond the mere fact that the fees are to come from the proceeds of the litigation, and take into account whether the support of the lawyer is supporting the litigation out of public interest or self-interest. This approach can be seen in the words of Millet LJ when he observed that "either it is improper for a solicitor to act in litigation for a meritorious client who cannot afford to pay him if he loses or it is not improper for a solicitor to agree to act on the basis that he is to be paid his ordinary costs if he wins but not if he loses. I have no hesitation in concluding that the second of these propositions represents the current state of the law" (at p 900). Thus, provided there is no fee inflation to take account of the contingency of losing the case, an arrangement whereby the fee is reduced or waived in the event of a loss is not illegal as contrary to public policy.

THE TORT OF CHAMPERTY

Under the current law a contingent fee arrangement under which the fees are inflated to take account of the risk of loss is champertous maintenance. It is also illegal as contrary to public policy. An action in champerty may be brought only by a person who has suffered wrong at the hands of the tortfeasor. If a party successfully defends a case against a plaintiff whose action was maintained by a champertous contingency fee (ie an inflated fee) an action will lie against the plaintiff's solicitors. The amount of damage would be the actual costs incurred in defending the claim.

Where a champtertously maintained action is successful (either by an award or by a settlement whereby the plaintiff receives some compensation) no action will lie. This is on the basis that there can be no damage in being required to

meet what are found, or admitted, to be existing legal obligations (*Sievwright v Ward*; Laws of New Zealand *Tort* para 181). It is also well established that where the action is supported through charitable or public interest motives (rather than self-interest as in the case of contingency fees) no wrong will be committed: *Sievwright v Ward.*

ILLEGALITY AND CONFLICTS OF INTEREST

The litigant who has entered into a champertous fee arrangement has no action in tort against the solicitor as no wrong has been committed against the litigant. However, as noted, an arrangement which is champertous is also illegal as contrary to public policy. It is therefore open to the litigant to refuse to pay the fee in the event of the litigation being successful on the basis that the contract is illegal and therefore void: Illegal Contracts Act 1970 s 6.

This fact makes entering into contingency fee arrangements ethically problematic for lawyers. By doing so they are putting themselves in a situation by which their interests are irreconcilably in conflict with those of their client. They are invoicing their client (and quite possibly deducting from the proceeds of litigation) fees which clients are not legally obliged to pay. Rule 1.03 of the Rules of Professional Conduct for Barristers and Solicitors provides that:

> A practitioner must not act or continue to act for any person where there is a conflict of interest between the practitioner on the one hand, and an existing or prospective client on the other hand.

This places the practitioner in the paradoxical position of having to decline to act where they have agreed to act under a contingency fee arrangement. It is also arguable that there is a duty on the practitioner to disclose the existence of the personal interest (ie the unenforceability of the fee arrangement) which gives rise to the conflict.

TAKING CHANCES

This writer is aware that a number of firms enter into fee arrangements in respect of litigation which are both conditional on success and inflated to take the risk of loss into account. Similar arrangements whereby the fee is discounted in the event of a loss and/or inflated in the event of a win are also frequent. Those arrangements are prima facie champertous and illegal. If this is pointed out to the firms the rejoinder is often that this is old law and not suited to modern conditions. It is, however, still the law. While there are some cases which may fall on the borders of the rule, of which *Thai Trading* was one, most clearly fall foul of the law.

Much may be said in favour of the move towards the mischief based approach anticipated by the English Court of Appeal in *Thai Trading*. However, a rule which is based on whether the arrangement is beneficial or detrimental to the operation of the legal system generally is a distant hope. To achieve such a rule in the near future legislation is needed, and advocated.

It is undeniable that the rules against maintenance and champerty are feudal in origin, and fit ill with the current conception of legal practice. There are good policy reasons for reforming this area of the law. However, until that occurs a lawyer who undertakes litigation pursuant to an arrangement under which no fee is payable in the event of a loss, and fees are inflated in the event of a win is committing a tort, entering into an unenforceable contract, and engaging in an ethically questionable practice. ❑

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continued from p 389

UK 1996 Act where a contract contained an arbitration clause, any subsequent claim made by one of the parties in relation to the contract which the other party refused to pay or admit, was a relevant dispute which the claimant was both entitled and bound to refer to arbitration, notwithstanding the fact that the respondent did not have a sustainable defence to it.

This ground for refusing to stay Court proceedings was considered recently by Master Kennedy-Grant in *Fletcher Construction New Zealand & South Pacific Ltd v Kiwi Cooperative Dairies Ltd*, High Court New Plymouth, CP 7/98, 27 May 1998, Master Kennedy-Grant. The plaintiff had sought summary judgment in reliance on three payment certificates issued in respect of three contracts entered into between the plaintiff and defendant. The defendant opposed the plaintiff's application on the grounds that it had an arguable defence, and that there were disputes in connection with the amounts claimed, which had been referred to arbitration and therefore the plaintiff's proceeding should be stayed under the Arbitration Act. The Court therefore had to consider whether there was a dispute between the plaintiff and the defendant within the meaning of art 8, and what the test was for determining whether there is a "dispute between the parties" in terms of art 8.

Counsel for the defendant submitted there was a dispute within the meaning of art 8 if the defence is advanced in good faith, whatever its chances of success. He submitted this approach was consistent with the view of New Zealand Courts that parties who have entered into an arbitration agreement should be held to it, and furthermore had been adopted in a number of English cases dealing with the equivalent provision in s 1(1) of the Arbitration Act 1975 (UK). Counsel for the plaintiff, on the other hand, submitted the correct test was that applied in summary judgment applications, namely whether there is an arguable defence. This was in line with the approach previously adopted in relation to s 5 of the Arbitration Act 1908, for example, in *Royal Oak Mall Ltd v Savory Holdings Ltd*, CA 106/89, 2 November 1989.

Master Kennedy-Grant referred to the Law Commission's discussion of this phrase at paras 308-309 of NZLC R20. The Law Commission had there noted the comments in the Mustill Committee's Report (1990) 6 Arb Int 53, that s 1(1) of the Arbitration Act 1975 (UK) was "of great value in disposing of applications for a stay by a defendant who has no arguable defence". Relying on the statements made by the Law Commission, Master Kennedy-Grant stated at p 13 of his judgment:

> I am satisfied that the test of whether there is a dispute between the parties for the purpose of Art 8(1) is not whether the party disputing liability is bona fide but whether it has arguable grounds for disputing liability.

This sensible approach may be contrasted with the current English position where, as noted above, there must be a reference to arbitration even if there is no sustainable defence: *Halki Shipping Corp v Sopex Oils Ltd.* ❑

The author will continue his consideration of the Arbitration Act 1996 in subsequent articles.

CHEQUES IN FULL SATISFACTION

TRANSACTIONS

edited by

Brian Keene

Magnum Photo Supplies Ltd v Viko New Zealand Ltd CA 82/98, 11 October 1998.

The Court of Appeal considered the law on accord and satisfaction and the effect of cheques sent in full satisfaction of a greater ostensible liability.

The High Court, (Cartwright J, M 606/95, 24 March 1998) held that a cheque for $124,677.18 sent by Viko to Magnum and inadvertently receipted and banked by its solicitor constituted an accord and satisfaction for a judgment in Magnum's favour of $275,450.85 entered in the High Court.

Viko, by its solicitors, proffered the cheque on 2 December 1997 with a covering letter, two crucial terms of which were –

> Presentation of this cheque will constitute acceptance of this offer. Should the offer contained in this facsimile be acceptable to Magnum, we look forward to your confirmation of that.

The letter was received on 3 December 1997. Instructions were sought from Magnum by its solicitors but before these were received, a legal secretary inadvertently receipted the cheque and arranged for the cheque to be banked at 4.00 pm that day.

The next day (4 December 1997), Viko's solicitors received the receipt in the mail and later the same day a facsimile advising that the receipt had occurred inadvertently and that the funds were held on behalf of Magnum and were available for return. There was an offer to verify inadvertence by an affidavit from the legal secretary involved.

Viko argued that the cheque was sent with a plain statement of the consequences of its being banked. That occurred and was acknowledged by the receipt sent. The offer had been accepted by action communicated to the offerer and accordingly there was a binding contract.

Magnum argued that it never intended to accept the offer and so should not have been bound by the mistake. It pointed that the alleged communication of the "acceptance" of the offer contained words on the receipt which would make it evident that there had been a mistake. The receipt described the amount of the cheque as "being Costs/Disbs as awarded by the Court". By any interpretation, it was clearly not that.

The Court of Appeal first ruled that the question of whether a contract had been concluded was a question of fact not law. It was to be determined on the basis of all the available evidence. It is permissible for an inference to be drawn from actions but again that inference can only be taken in the light of all the evidence and not just parts of it.

Crucially, the Court then determined that it was common ground that Magnum did not intend to agree to the terms of the settlement proposed. On that basis, the Court decided that there was no intention to accept the offer. In forming this view, the Court did not have regard solely to the actions and communicated advice but rather the "real" situation which developed because of Magnum's solicitor's mistake. The objective actions being the receipt of the money and banking it on their face, appeared to be an acceptance. However, the Court of Appeal took a literal interpretation of the phrase "presentation of this cheque" appearing in the letter of offer. It held –

> "Presentation" of the cheque could be interpreted in its strict meaning of presentment to the Bank on which it was drawn for collection or, as Mr Fardell contended, simply as banking that is depositing for collection. The issue and posting of the trust account receipt indicated neither. It merely acknowledged receipt of the cheque and demonstrated an intention to deposit it at a future point so as to collect the funds. The solicitors for Viko had no notification of the banking or presentment of the cheque until that was received contemporaneously with advice in the same letter that there was no intention on the part of Magnum to accept the offer.

One worries that the Court of Appeal may be entering in the difficult area of establishing the contract not by virtue of the objective communicated actions of the parties but more by their subjective intent. There are obvious dangers in such an approach, not the least of which is continuing commercial uncertainty surrounding the transaction.

Postulate, for example, that nothing more occurred for some days other than the issuance of the receipt and the banking of the money. At what point, would contractual certainty have been achieved? If it requires communication formally confirming the banking in terms of the offer, then the stipulation of mode of acceptance of the offer is effectively defeated. If such practices abound, they are generally seen as giving quick fire solutions where parties, by their actions, opt to take lesser payments for the benefit of having the money.

Whilst the decision gives a comforting feeling of justice to Magnum, that is at the expense of commercial certainty both in the particular case and generally in this area of cheques in full satisfaction.

LAW REFORM: RETIREMENT VILLAGES

The Law Commission has recently issued a Discussion Paper on retirement villages inviting comments on a proposed law reform package. It is a curious ad-mixture of sophistication of analysis and simplicity of solution which may, in the end, prove less effective than the current regime.

There are a multitude of arrangements which are popularly known as retirement villages. The present regime under the Securities Act 1978 may catch some and not others. The report wisely observes –

> It was never satisfactory that the [Securities Act] should apply to some retirement villages and not to others. The concern of the Securities Act is the management of the risk that is an inseparable part of the trade and security. This is an inappropriate approach to the protection of senior citizens who take up residence in retirement. In their case the concern should not, as in the case of traders, be to manage the risk but should be first to reduce the risk to the extent possible and secondly to warn of any remaining hazards.

The analysis proceeds to deal to detail two principal areas of risk management:

- first, the acquisition of the occupation right which is typically associated with a substantial capital payment;
- second, the maintenance of the range of services for residents envisaged by the scheme of lifecare at the time of an individual's acquisition of his/her occupancy right.

At present, some retirement villages function under the aegis of the Securities Act. For those Villages, there is a set regime under an Exemption Notice which makes specific provision for the management of both risks. In essence, depending upon the nature of the security offers, prospectus-type information with a continuous process of financial audit satisfies the key information requirement.

The Law Commission's solution may be thought worryingly simple. It involves –

- a "robustly expressed warning".... in terms as trenchant as [the Law Commission] can persuade the legislature to agree to;
- the appointment of a "Prudential Supervisor" who would not only settle the form of the notice but also lay out the rights and liabilities of the residents in a succinct and lucid form;
- the Prudential Supervisor would be liable to the resident for any loss arising from any inadequacy in disclosure;
- both the Prudential Supervisor and the Registrar of Companies would be given certain powers to apply to the High Court to cover any case where circumstances arose calling for the protection of residents' rights by the Court;
- disputes between residents and the retirement village owner would fall under the jurisdiction of the Tenancy Tribunal.

Some questions may arise concerning the Law Commission's proposed solution. They are, in no particular order –

Arguably, the callow youth buying his first apartment is more likely to fall into error than a 60-70 year old acquiring his/her fourth or fifth permanent residence

THE CASE FOR SPECIAL PROTECTION

Unarguably, residents acquiring occupation rights in a retirement village should be in a no worse position than persons who acquire comparable rights and securities under the Securities Act. However, the Commission comments upon the risks of under-capitalisation of the developer with the potential risk that the full extent of a proposed site development may not eventuate. This carries the prospect of higher ongoing costs shared amongst few residents. Those risks differ little from similar risks run by a purchaser of an apartment in an apartment complex or a strata title office within a larger building. Neither of these require a complex disclosure regime because of s 5(1)(b) of the Securities Act. As the report notes, many retirement village developers have chosen to adopt a similar mode, no doubt for simplicity and cost saving reasons. The proposed Bill will put an end to that with the, no doubt, consequential increased compliance cost problem.

The proposition advanced in para 21 of the report that because the purchasers are "ex hypothesi" elderly, there is a stronger case for protection may not withstand much scrutiny. Age very often brings wisdom and experience and not always frail unworldliness. Arguably, the callow youth buying his first apartment is more likely to fall into error than a 60-70 year old acquiring his/her fourth or fifth permanent residence.

THE REALITY OF THE PROTECTION

The report correctly identifies both the capital commitment to and the ongoing viability of the retirement village as being a prospective resident's largest potential risk. How well does the Commission's solution protect each of those?

First one must say that the capital cost once expended is generally recovered by an on-sale by the resident or his/her Estate. That sale price will reflect a number of environmental factors such as geographic supply and demand. Most fundamentally, a new purchaser will seek to know the quality and stability of the then current management of the Village. New residents will wish to be reassured that their investment is safe and they will enter into a well managed and stable community.

It is in this context that the trenchant warnings from the Prudential Supervisor and the ability for the Village scheme to come under the control of the Registrar of Companies may be seen as less than a subtle solution. Such steps may very well be a cure worse than the disease. The very protection relied upon may indeed become the primary cause of the resident's actual loss.

THE PRUDENTIAL SUPERVISOR

If you add the proposed roles and responsibilities of the Prudential Supervisor, there may be created a wholly volatile mix. Consider the component parts.

First, the Commission discounts the probability that prospective residents themselves will read and understand the detailed information up to now required by the Exemption Notices issued under the Securities Act. Describing the document so produced as "The Reverse of Lucid", the Commission observed –

> But experience clearly demonstrates that prospective purchasers tend to be impatient of Prudential considerations. They are likely to be most influenced by the location of the Village or the proposed Village, by description of amenities and by the fact that their friends are already residents or plan to be. They are likely to be unimpressed by expanses of fine print or polite recommendations, courteously conveyed by their solicitors or accountants, not to proceed. If disclosure is to be effective, something more direct and outspoken is needed.

Thus expressed, the paternalistic nature of the legislation is evident. Pity, however, the poor Prudential Supervisor whose task is to be persuasive where the Commission feels, up to now, the close commercial advisers of elderly residents have failed. Pity him/her the more so as the message must be conveyed directly succinctly and in an outspoken way.

One presumes a good statutory supervisor will wish to maintain a reasonable balance between working with and encouraging the retirement village operation and being forthright and outspoken concerning the business risks for prospective residents. All the time, the supervisor must be aware that the hotter he blows about the risks, the more likely is he to depress the value of existing residents' investments. The more restrained he is, the greater is his risk of being sued by a new resident coming in, situations of loss occurring and the supervisor, by the exquisite process of hindsight, being deemed irresponsible by the Courts.

It is this risk of suit that underpins a deal of the reasoning of the report. Although elegantly proposed, is it anything more than a risk transference device taking off the shoulders of those responsible for the decision the need to make full inquiries and placing it upon a paid functionary to act as a quasi insurer of those not able or bothered to adequately weigh up their investment decision?

COMPLIANCE COSTS

The Commission's report suggests that the initial documentation under its proposed regime will be less complex and therefore cheaper than is currently the case under the Securities Act. One wonders whether that prognosis will prove correct.

> ***For every risk undertaken, there is usually a cost to the party relieved of the burden. The Supervisors themselves are likely to seek indemnity insurance and cost that into their fee.***

First, as the report acknowledges, the majority of retirement villages have structured themselves so as to avoid the compliance costs of the Securities Act. It is only the well-capitalised, well-run operators who have seen the benefits of the prospectus regime and have adopted them. For the other small and medium scale establishments, compliance costs under the new regime will undoubtedly be higher than before.

Secondly, compliance costs will be influenced by the degree of information required by an individual Prudential Supervisor. The clear message from the Draft Bill is that inadequacy of disclosure causing loss may lead to a suit against the Supervisor. One would expect persons taking up that role to require significant on-going and verified information to protect themselves against that risk.

Thirdly, the compliance costs will be influenced by the quasi-insurer role which the Supervisors will take on. For every risk undertaken, there is usually a cost to the party relieved of the burden. The Supervisors themselves are likely to seek indemnity insurance and cost that into their fee. In the end, will the new regime be cheaper?

THE DRAFT BILL

Those advising clients in the area, be they developers or actual or potential elderly residents, would do well to consider the ramifications of the Bill upon existing and future retirement villages. For many of them, new costs will be incurred in the appointment of Supervisors and the compiling and management of new information. What will those costs be and will they constitute value for money? How the new Bill applies to existing Village developments is somewhat uncertain and will probably need to be clarified before the Bill is finally passed (if it is).

The Commission in its desire to capture "all" retirement villages, has created a set of wide definitions under which a residential complex which in fact attracts predominantly retired persons could be deemed to be a retirement village even though it would not be so described in common parlance.

The obligations of the Statutory Supervisor are not spelt out. Perhaps this is purposeful. Unless some information needs are set out either in the Act or in Regulation, there is a real risk of wide variation between the information supplied depending upon the instinct of the Supervisor. The Commission's report remarks upon the undesirability of the Securities Act applying to some Villages and not others. By a parity of reasoning, such variations are undesirable.

CONCLUSION

There is little doubt that retirement villages are not easily bought under the Securities Act disclosure regime. It may be desirable to have separate legislation although the case is far from clear cut. Whether the Commission's proposed solution is workable and subtle enough to provide an adequate solution may be an open question.

One trusts that the Commission will listen carefully to all sectors. Whilst the elderly resident or potential resident may wish to improve his/her legal protections, the experience of the retirement village operators and those organisations who have taken up roles as Statutory Supervisors under the Securities Act should be carefully considered. It is in their interests to foster not only their industry and professional objectives but also the desirability and viability of retirement villages. It is, after all, from that source that they gain their livelihood and the promotion and protection of that industry is as important to them as it is to residents.

Submission on the Discussion Paper are open until 28 February 1999.

VOIDABLE PREFERENCE: "ORDINARY COURSE OF BUSINESS"

In *Re Anntastic Marketing Ltd (In Liquidation)* M 468/97 High Court, Auckland, Baragwanath J, 9 September 1998, the Court was called upon to consider s 292 of the Companies Act 1993 allowing it to set aside voidable transactions.

The liquidator had taken three test cases to the Court. Each of the applicants had received moneys from Anntastic within six months of its liquidation. The Court found as a fact that over the relevant period, Anntastic was insolvent. Therefore, moneys received could only be retained if the beneficiary could demonstrate such transactions took place in the ordinary course of business as defined in s 292(2) and (4).

Baragwanath J opened his careful judgment by observing the need to balance the two public policy imperatives of first ensuring that all creditors are dealt with equally on the winding up yet second suppressing the risk of impairing the free flow of trade by undoing reasonable transactions because of a subsequent liquidation. His method of achieving that balance was to define the circumstances in which the transaction takes place in the ordinary course of business.

Section 292(4) of the Companies Act 1993 statutorily excludes the intent of the company to prefer a particular creditor or advance his/her interests as being relevant to the ordinary course of business test unless that intent was known to the beneficiary. Obviously, were it known, an arrangement to exploit that becomes tantamount to bad faith viz a viz other creditors.

However, aside from those particular restrictions, how is the Court to interpret "ordinary course of business"?

> The matter is in my view to be viewed from the standpoint of an objective observer having the knowledge possessed by the trader of any previous course of dealings by the company and any relevant practices within the industry.

This formulation contrasts with the Privy Council's view in *Countrywide Banking Corporation v Dean* [1998] 1 NZLR 385 –

> The transaction must be such that it would be viewed by an objective observer as having taken place in the ordinary course of business. While there is to be a reference to business practices in the commercial world in general, those focus must still be the ordinary operational activities of businesses as going concerns, not responses to abnormal financial difficulties ....

The Privy Council cited, with approval, Fisher J in *Modern Terrazzo Ltd* [1998] 1 NZLR 160 at 175 –

> Whether a payment should be regarded as commercial routine at a day-to-day trading and operating level will turn at least in part upon a comparison with the practices of the commercial community in general. But equally, the way in which the particular company has acted in the past and its dealing with the particular creditor, would seem pertinent.

It is also worth observing that the former jurisprudence was driven by the provisions in the 1955 Act which required the Court to have regard to whether the imprudent transaction was entered into "with a view to", altered by the 1993 Amendment Act. Now the sole protection left to a beneficiary is the "ordinary course of business" test without any regard to intention or proposed effect.

Baragwanath J reviewed three transactions. Two of them he decided unequivocally were within the ordinary course of business. In both of those cases there was both an absence of knowledge of financial difficulty of the subject company and a quite normal pattern of following up and securing payment for accounts either due or overdue.

The third case involved a total payment of $25,000 in three tranches of $10,000, $5000 and $10,000. The cheques covered orders of picnic hampers where the contracted payments were in three tranches commencing 11 October 1996 and ending 15 November 1996. The first payment was made in time but a second payment of $15,000 on dispatch of the hampers was not received. Further supply was then withheld. A cheque for $13,687.50 was delivered on 11 November for presenting on 20 November. However, on 15 November, the supplier was advised of a dispute concerning quality. There was an immediate stop on the cheque due to be presented on 20 November. There was, at that time, no suggestion of financial difficulty. The quality dispute was ultimately resolved and appeared to be the responsibility of a third party. On 26 November a further cheque for $10,000 was paid following which further deliveries of hampers were made.

Baragwanath J upheld all payments as being in the ordinary course of business except for the $10,000 paid on 26 November. He ruled:

> I uphold the liquidator's submission that the pickle factory must have known that it was no longer safe to rely on the terms of the contract in order to extract the $10,000 on 26 November 1996 and therefore impose such pressure of withholding supply that the payment was made and received outside the ordinary course of business.

Section 296 of the Companies Act 1993 provides that a liquidator may not make recovery if a person from whom it is sought received the property in good faith and altered his/her position in a reasonably held belief that the transfer was validly made and would not be set aside. The judgment records that no reliance was made upon that section but such a claim would not have been sustained.

It has been commonly thought that a remedy which any creditor has is to withhold supply against payment, particularly, as here, the time for payment has passed. Supply resumes when payment is made. The effect of this decision puts such arrangements into question where a creditor knew or ought to have known that the company was insolvent. This leaves the unsatisfactory situation that to continue with the contract on payment of the cash sum will cause a creditor to be at risk if the transaction is avoided. The only choice is to withhold supply utterly which is an unsatisfactory and uncommercial solution.

It is not immediately clear why s 296 could not be invoked. However, what is apparent is that in circumstances where there are grounds for the creditor to believe that the company is insolvent, there is a substantial risk that a payment received, even in good faith, may be recaptured by liquidators. ❑

COMPULSORY CAESARIAN SECTION

Nicola Peart, University of Otago

discusses R v Collins *and its implications in New Zealand*

R v Collins, ex parte S [1998] 3 All ER 673 is a recent decision of the English Court of Appeal, in which patient autonomy was strongly reaffirmed. The appeal set aside a High Court order which authorised a compulsory caesarian section on a pregnant woman against her express wishes. The Court of Appeal also granted relief by way of judicial review against the respondents in respect of their decisions to apply ex parte for the woman's compulsory admission under the Mental Health Act 1983.

FACTS

Ms S was a 29-year-old who became pregnant in September 1995. She did not seek ante-natal care until 25 April 1996 when she was approximately 36 weeks pregnant. She then registered as a new patient with Dr Chill, a GP, who diagnosed her as suffering from severe pre-eclampsia, a disorder of pregnancy which manifests itself in high blood pressure with potentially fatal consequences for both mother and child. Dr Chill advised immediate admission to hospital and an induced delivery. S refused, because she wanted to have her baby naturally, in a barn in Wales. She did not care about the risks to herself or to her unborn child and thought it would be better for the baby if it died.

Concerned about S's mental state, Dr Chill called in an approved social worker, Miss Collins, and a psychiatric Registrar, Dr Jeffreys. They tried to persuade S to go to hospital for treatment, but she was adamant in her refusal. Miss Collins felt that she had no choice but to detain S "for assessment" in accordance with s 2 Mental Health Act 1983. Dr Chill and Dr Jeffreys provided the necessary recommendations. S was admitted to hospital where the seriousness of her condition was confirmed.

S continued to refuse treatment and was advised by a solicitor that she was entitled to do so. The hospital made an ex parte application to the Family Division of the High Court for a declaration authorising a caesarian section. Neither S nor her solicitor knew anything about this application.

The application came before Mrs Justice Hogg on 26 April. On the basis of the information given to the Judge, including the incorrect fact that S had been in labour for 24 hours, Hogg J granted the declaration within half an hour. Later that day, when the foetus became distressed, an emergency caesarian section was performed and S gave birth to a healthy daughter.

On 30 April S was seen by another psychiatrist who found no evidence of mental illness. Her detention was terminated. S left hospital alone, rejecting the baby at first, but later decided to keep her.

THE PROCEEDINGS

After her discharge S commenced proceedings in public law and in private law against the social worker and the Health Trusts where she had been treated. Her application for judicial review was lodged outside the time limit, but the Court of Appeal considered the issues of such public importance that it granted leave to move for judicial review. ([1998] 1 FLR 790) Aware that S was also appealing against Hogg J's declaratory order, the Court took the unusual step of joining the two proceedings.

THE DECISION

S succeeded in both proceedings. The Court of Appeal was critical of virtually every step of the medical and legal procedures which had been employed to detain and treat S against her express wishes. The main issues of concern were:

1. the principle of autonomy and its application to pregnant women;
2. the use of Mental Health legislation, and
3. the use of ex parte applications for medical or surgical treatment.

The autonomy principle

The Court of Appeal reiterated the fundamental principle that an adult of sound mind is entitled to refuse medical treatment even when his or her own life depends on it. This principle applies equally to competent pregnant women:

> In our judgment while pregnancy increases the personal responsibilities of a woman it does not diminish her entitlement to decide whether or not to undergo medical treatment. Although human, and protected in a number of different ways ..., an unborn child is not a separate person from its mother. Its need for medical assistance does not prevail over her rights. She is entitled not to be forced to submit to an invasion of her body against her will, whether her own life or that of her unborn child depends on it. Her right is not reduced or diminished merely because her decision to exercise it may appear morally repugnant. (p 692)

Unless there was a lawful justification, such as incompetence, as was the case in *re MB* [1997]2 FLR 426, the compulsory caesarian section infringed S's autonomy.

The Mental Health Act 1983

The Court found that S was not incompetent. Her capacity to consent was intact. Her thinking process was unusual, even apparently bizarre and irrational, and contrary to the views of the overwhelming majority, but the Mental Health Act could not be deployed to detain people against their will

on those grounds. (p 692) She was detained to treat her physical condition, not her mental disorder. In fact she never received any treatment for her mental condition. The application under the Mental Health Act was therefore unlawful and S's autonomy was infringed.

The ex parte application

The Court found the procedure before Hogg J "so extraordinary and unfortunate" that it felt bound to restate some fairly elementary points about declaratory relief, and provide guidelines for the future. (p 699) It was particularly concerned by the fact that these proceedings had been taken ex parte and without full investigation of the merits.

The Court condemned the use of ex parte applications in these sort of cases, because they are unjust and any resulting declaration would not achieve its purpose. S had not been given notice of the proceedings nor an opportunity to be heard and she was therefore not bound by the order.

Moreover, the application did not fully and frankly disclose all the material facts. Hogg J was told that S was in labour when she was not, and was not told that S's capacity appeared intact, that she had contacted a solicitor and that she had no knowledge of the application. The appeal was allowed and the order was set aside. The caesarian section thus constituted a trespass, rendering the respondents liable to a claim for damages.

THE NEW ZEALAND SCENE

It seems unlikely that a case like *R v Collins* would occur in New Zealand today. The right of a competent adult to refuse medical treatment is also part of our common law, but it is reinforced by s 11 NZ Bill of Rights Act (1990) and Right 7(7) Code of Health and Disability Services Consumers Rights. (Code of Rights.) Besides, the considerable attention given to patient rights since the Cartwright Inquiry in 1988 can leave few health professionals in doubt about the importance of patient autonomy.

The application of this right to pregnant women has not been judicially tested here, but it seems unlikely that their right to refuse treatment will be curtailed in the interests of their unborn children. *R v Collins* reaffirms that a foetus has no separate existence from its mother. The mother's autonomy is determinative until the child is born alive. To accord a foetus rights which restrict the mother's autonomy creates fundamental moral and legal problems. It is a slippery slope with no obvious stopping point.

To go down this slope is nonetheless tempting, particularly when the foetus is viable. A woman's refusal of common treatment in such circumstances seems morally repugnant. Courts overseas have occasionally succumbed to this temptation and overridden the mother's right to refuse treatment in the interests of the unborn child. (England: *Re S* [1993] 1 FLR 26; US: *Jefferson v Griffin Spalding County Hospital Authority* [1981] 274 s 2d 457; *In re Madyyun* [1986] 573 A 2d 1259; Canada: Schulman J in *Winnipeg Child and Family Services Ltd v DFG* [1996] 10 WWR 95 (QB).)

However, they have generally reverted to the principle of patient autonomy, finding no rational or morally acceptable basis upon which to limit this fundamental right of competent adults. In the light of this experience, it seems improbable that a New Zealand Court would override a competent woman's refusal of treatment, no matter what the consequences to the woman or her unborn child.

The New Zealand Mental Health (Compulsory Assessment and Treatment) Act 1992 is similar to the English Act. Its purpose is to treat a person's mental condition, not her physical condition. If the competence of a person with a physical illness is in question an application under the Protection of Personal and Property Rights Act, or under the parens patriae jurisdiction, would be possible, though neither will succeed if the person merely has unusual views. Even if her competence were diminished by a mental disorder, she would still retain the right to give informed consent to treatment to the extent of her competence. (Right 7(3) Code of Rights) The principle of autonomy is thus extensively protected in New Zealand.

REMEDIES

Health professionals in New Zealand may be treated less sympathetically than their peers were in England. If a case like *R v Collins* were to arise here, the most likely course of action would be a complaint to the Health and Disability Commissioner alleging a breach of the Code of Rights. The complaints procedure is laid down in Right 10 of the Code and in Part IV of the Health and Disability Commissioner Act (1994). It is a cheap and simple procedure potentially culminating in a hearing before the Complaints Tribunal. (s 45) The Tribunal has the power to grant one or more of a range of remedies, including an award of damages. (ss 54 and 57) However, as the performance of an unlawful caesarean section would constitute a medical misadventure under s 5(6) Accident, Rehabilitation, Compensation and Insurance Act 1993, the Tribunal would have no power to award compensatory damages. (s 52(2) H&DC Act)

Punitive damages would still be a possibility. Section 52(2) Health and Disability Commissioner Act expressly provides for this if the conduct of the health provider was "in flagrant disregard of the rights of the aggrieved person". (s 57(1)(d) H&DC Act.) The Court in *R v Collins* commented that this was not a case where such an award would be appropriate. The respondents were all motivated by a genuine desire to do what was best for S and her unborn child in extremely difficult circumstances. (p 694) Such a benevolent view may be less likely in New Zealand.

A breach of the Code of Rights may also be referred to the relevant health professional body for disciplinary action. (s 45 H&DC Act) Doctors who claim that a woman was incompetent to refuse treatment in the face of clear evidence to the contrary may well be disciplined by the Medical Disciplinary Tribunal.

Criminal prosecution is another option. The performance of a caesarean section against the patient's express wishes is an offence against the person. A charge of wounding or injuring with intent (ss 188 and 189 Crimes Act) may be difficult to defend under ss 61 and 61A Crimes Act, because the operation would have been unreasonable in the light of the woman's express refusal. However, given the range of alternative proceedings already described, a criminal prosecution would seem to serve little purpose.

CONCLUSION

While a case like *R v Collins* seems unlikely in New Zealand, it is nonetheless a salutary warning to health professionals that no matter how unreasonable patients' decisions may be, their right to refuse medical treatment is sacrosanct unless they lack the necessary competence at the time of making that decision. Any attempt to interfere unlawfully with that right may result in legal and disciplinary action which is considerably less forgiving than the Court of Appeal was in *R v Collins*. ❑

THE RWANDA TRIBUNAL

Sarah Murphy, Ministry of Justice

reports on the International Criminal Tribunal for Rwanda

In 1994, Security Council Resolution 955, set up the International Criminal Tribunal for Rwanda ("the Tribunal"). This is the fourth international criminal tribunal, the International Military Tribunal at Nuremberg was set up in 1945; the International Military Tribunal at Tokyo in 1946, and the International Criminal Tribunal for the Former Yugoslavia in 1994. Its creation has strengthened the legal principle developed at the time of the Nuremberg Tribunal that the perpetrators of genocides and crimes against humanity are accountable to the international community. The establishment of the Rwanda Tribunal only a year after the Yugoslavia Tribunal was also a crucial step towards the agreement by states in July this year to a statute creating a permanent International Criminal Court.

Some commentators are cynical about the creation of the Tribunal, in light of the failure of the United Nations to prevent the 1994 massacres, in which an estimated one million Tutsis and politically moderate Hutus were murdered. Nevertheless, the establishment of the Tribunal under Chapter VII of the UN Charter has forged an important link between domestic human rights violations, international peace, and justice. This, together with an expansive definition of international offences has afforded the Rwanda Tribunal the potential to be an important instrument in enhancing future respect for human rights, and in encouraging the international prosecution of grave crimes.

Regrettably, in spite of the Tribunal's progressive constitutional roots, it has laboured under resourcing constraints and a tense relationship with Rwanda. In that context, it has struggled and at times failed, to match principle with practice. In particular, it has on occasion failed to adhere to its own Rules of Procedure and to maintain certain basic international legal standards of criminal procedure.

CONSTITUTIONAL STATUS OF THE TRIBUNAL

The Tribunal was created by the Security Council under Art 41 of Chapter VII of the UN Charter. The use of Art 41 (which empowers the Security Council to take non-military measures to maintain or restore peace) required a determination under Art 39 of the Charter that the circumstances in Rwanda required measures to be taken to "maintain or restore international peace and security".

In determining the Rwanda situation to be a matter of "international peace and security" in terms of Art 39, the Security Council significantly developed the precedent created by its decision to set up the Yugoslavia Tribunal. While both Tribunals were set up under the same provisions, the abuses in the former Yugoslavia took place in an armed conflict, which was of international character, and therefore the link between the Tribunal and the maintenance and restoration of international peace was apparent. In contrast, in Rwanda the genocide was largely domestic, and not clearly within the context of an armed conflict, so the relationship between the Tribunal and international peace required a more subtle analysis. In creating the Rwanda Tribunal the Security Council therefore broke ground by acknowledging a link between domestic human rights abuses, international peace, and justice. The abuses were so severe that they were seen to endanger regional and international peace. The creation of a Tribunal was a way to demonstrate international condemnation of those atrocities, and to deter future such peace-threatening acts.

THE STATUTE

The statute of the Rwanda Tribunal is progressive in its definition of offences. It is empowered to prosecute genocide, crimes against humanity, and war crimes. While largely based on the Yugoslavia Tribunal's statute, it differs in two significant ways, both of which represent advances in international law. Its definition of war crimes expressly includes war crimes committed in internal armed conflict (ie serious violations of Art 3 common to the Geneva Conventions of 12 August 1949 for the Protection of War Victims, and of Additional Protocol II of 8 June 1977). These provisions represent an evolving norm of international law which had not previously attracted individual criminal responsibility. This was a significant development, particularly as the majority of armed conflicts are now internal, and such conflicts are ready arenas for the commission of atrocities.

The Rwanda Statute's definition of crimes against humanity is also broader than that of the Yugoslavia Tribunal, which requires crimes against humanity to have been committed in the context of internal or international armed conflict (Art 5). The Rwanda Statute simply requires the acts to have been committed "as part of a widespread or systematic attack against any civilian population" (Art 3). The Rwanda Statute has therefore helped to settle a rule of customary international law that crimes against humanity do not require a nexus to armed conflict (confirmed in Art 7 of the Rome Statute of the International Criminal Court), which the Yugoslavia Statute might otherwise have undermined by requiring such a nexus.

CONCURRENT JURISDICTION

The preamble to Resolution 955 expresses one of the expected goals of the Tribunal as being to "contribute to the process of national reconciliation and to the restoration and maintenance of peace". Its ability to effect national reconciliation in Rwanda was, however, rendered difficult from the outset by the lack of support from the Rwandese government: the Rwandese delegate to the Security Council cast the only dissenting vote against the Resolution.

One of the difficulties the Tribunal faces, which restricts its ability to effect national reconciliation, is its concurrent jurisdiction with the Rwandese judicial system. The representatives of the victims of the massacres, the Tutsi backed Rwandese Patriotic Front, are now in power, and are anxious to prosecute high profile suspects. There has been significant rivalry between Rwanda and the Tribunal as to jurisdiction. While Art 8(2) of the Statute gives the Tribunal primacy, the Tribunal has found it difficult to persuade the Rwandese government to allow it to try suspects.

Differences between the jurisdictions result in the leaders of the massacres (who are generally tried by the Tribunal), receiving more favourable treatment than the less culpable players tried in Rwandese judicial system. The most significant difference between the jurisdictions is that the Rwandese Criminal Code allows for the death penalty, while cl 23(1) of the Rwanda Statute limits the Tribunal's sentences to imprisonment. The exclusion of the death penalty was a key reason that Rwanda did not support Resolution 955, and contributes to the tension between the two jurisdictions. The contrast between the sentencing processes of the two jurisdictions for those found guilty of genocide came to the fore this year. In April, 22 people convicted by the Rwandese Courts were executed, while in September, the Rwanda Tribunal, in its first sentencing decision, sentenced the former Prime Minister Jean Kambanda to life imprisonment.

ADMINISTRATIVE DIFFICULTIES

From the outset, the Tribunal has faced administrative hurdles. The Tribunal is based in three countries and two continents. The seat of the Tribunal is in Tanzania, the prosecuting office is in Rwanda, and the prosecutor is based in the Hague. The prosecutor is shared with the Yugoslavia Tribunal. This enhances cohesion between the two bodies, but also puts them under strain due to her limited availability. There have also been resourcing problems deriving from small and short-term appropriations from the General Assembly, which have been insufficient, in spite of some voluntary donations by states (including New Zealand) in accordance with Cl 4 of Resolution 955. Mismanagement of the Tribunal, reported on by the UN Office of Internal Oversight Services in February 1997, resulted in the resignation of the Registrar and Deputy Prosecutor.

FAILURE TO MEET UN MINIMUM STANDARDS

There have been delays in many aspects of the Tribunal's processes. Under Art 9(3) of the ICCPR "anyone arrested or detained on a criminal charge shall be brought promptly before a Judge or other office authorised by law to exercise judicial power". Principle 37 of the UN Body of Principles for the Protection of All Persons under Any Form of Detention or Imprisonment ("the UN Body of Principles") contains similar provisions. The Rwanda Tribunal's Rules of Procedure mirror these provisions. This principle has been interpreted by the United Nations Human Rights Committee as requiring "delays [not to] exceed a few days" (General comment no 8, para. 2, UN Doc. CCPR/C/21/Add.1). In spite of this, there have been several cases of detainees not being brought before a Judge for several weeks, and in one case, almost six months. There have also been unreasonable delays in indicting suspects, and in hearing motions, for example for the release of detainees, the protection of witnesses and the disclosure of evidence. (International Criminal Tribunal for Rwanda: Trials and Tribulations April 1998 AI Index IOR 40/03/98 Distr:SC/CO/IGO/PG)

Under Art 20(4) of the Rwanda Statute (and Art 14(3)of the ICCPR) trials must be held without "undue delay". In spite of this requirement, some defendants have been awaiting trial in custody for over 30 months. (In New Zealand, incarceration for that length of time prior to trial could potentially justify an acquittal; see eg *Martin v Tauranga District Court* [1995] 2NZLR 419.) A contributory factor to these delays has been long periods during which the Tribunal has been in recess (three months from June to August 1997 and six weeks during the 1997/98 Christmas period), an amount of time which has been described as "inexcusable" by Amnesty International.

The situation in the concurrent Rwandese criminal justice system is also extremely concerning: approximately 100,000 suspects are currently awaiting trial in overcrowded jails. These delays in both jurisdictions have led to the perception that justice is not being achieved, which has the potential to inflame a volatile political climate in Rwanda.

There have also been delays in the hearing of motions, including an extremely urgent motion filed by the lawyer for defendant Georges Rutaganda. The motion sought an urgent teleconference deposition for 16 defence witnesses, because of the endangered state of the refugee camp in Eastern Zaire in which they were living. The application was made on 17 February 1997. The motion had not been heard by 2 March, at which stage the camp was attacked and the witnesses disappeared. This absence of these defence witnesses will inevitably jeopardise the accused's right to a fair trial.

The Tribunal has also failed to meet international standards in its incarceration of Jean Kambanda. UN standards require that detainees are held in places which are officially recognised as places of detention (see, inter alia Principle 16(1) of the UN Body of Principles, art 10 of the Declaration on the Protection of All Persons from Enforced Disappearance, Human Rights Committee General Comment no 20, para 11, UN Doc CCPR/C/21/Add 6). Although documents pertaining to Kambanda's imprisonment record him as having been held in the Rwanda Tribunal's official detention unit, he has in fact been held in a secret location (reported to be a holiday residence for Tanzanian officials) due to purported security risks. While the Tribunal has said that there has been a visit to the site by the International Committee for the Red Cross, the lack of transparency surrounding the facility nevertheless risks the defendant facing harsh or lenient treatment. Although there may have been legitimate security considerations behind the transfer, such concerns should be addressed by tightening security at the existing facilities rather than ultra-vires arrangements.

CONCLUSION

The Tribunal is charged with a difficult task, in trying conditions and under resource constraints. The Tribunal and the international community have a joint responsibility to ensure that it does not betray its progressive constitutional roots and jurisdiction by ongoing breaches of international standards. Governments need to keep it fully financed, as this is critical if it is to minimise delays and otherwise fulfil its functions effectively. The Tribunal, too, must take steps to rectify all its processes so that all UN minimum standards are adhered to. These measures need to be taken to ensure that international standards of criminal procedures are maintained, the Tribunal's shortcomings do not discourage states from ratifying the International Criminal Court, and that it achieves its most important goal of enhancing national reconciliation in Rwanda. ❑

REGISTRATION ON THE INTERNET: WHOSE DOMAIN?

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comment on the English Court of Appeal decision on cybersquatting

A recent opinion of Aldous LJ (Swinton Thomas and Stuart-Smith LJJ concurring) has confirmed that systematic registration of well-known trade names on the Internet as blocking registrations can be passing-off [*British Telecommunications v One in a Million Ltd*, Court of Appeal 23rd July 1998] available at http://www.smithbernal.com/casebase_frame.htm. This opinion will bring great joy to the five large British companies who originally sought the injunction, and to the other owners of trade names, trademarks and brands (hereinafter trade names) who will free ride on the outcome, perhaps unaware of the irony that their ability to free ride has arisen from the Court's condemnation of free riding in the first place.

The circumstances which gave rise to the original action (heard before Mr Jonathan Sumption QC, sitting as deputy Judge of the High Court, 28 November 1997) were that various dealers in Internet domain names had registered well-known trade names, such as Virgin, having no connection with those trade names. The plaintiffs, five large companies which owned some of the trade names which had been so registered, had sought injunctive relief under s 10(3) of the Trade Marks Act 1994 on the grounds that such registration constituted infringement, as the domain names were intended to be used in the course of trade and were identical or similar to their trademarks. Mr Jonathan Sumption QC had found for the plaintiffs and granted relief. The defendants had then appealed on three grounds. First, registration could not be an instrument of fraud where several companies might, or already did, use the trade name in question. Second, even if they did have the intention to sell the registration to another company which would to their knowledge engage in passing off the names as those of the registered owners, mere assistance was not sufficient, and they would not be identified as the party who did the passing off. And third, to infringe s 10(3), there had to be use of the mark and the use had to be the use of a trademark as a trademark in relation to goods and services.

His Lordship was of the opinion in relation to the first issue that all circumstances had to be taken into account in assessing whether any name was an instrument of fraud, including "the similarity of the name, the intention of the defendant, the type of trade and any other relevant factors". He made a distinction between the trade name Virgin where there might be room for doubt on the issue of uniqueness, and Marks and Spencer where there could no such doubt. Nevertheless, he found evidence of systematic registration by the appellants of well-known trade names as blocking registrations and a threat to sell them to others. He found the deliberate practice, over a substantial period of time of registering domain names chosen to resemble names and marks of other people plainly intended to deceive. He found the registration of the names by the appellants were instruments of fraud. It was the value of the goodwill, not the fact that they could by used by a third party which caused the appellants to register the names.

On the second issue, His Lordship found that "If, taking all the circumstances into account the Court should conclude that the name was produced to enable passing-off, was adapted to be used for passing-off, and, if used, was likely to be fraudulently used, an injunction would be appropriate". He therefore dismissed the argument.

On the third, His Lordship was of the opinion that "...[he] was not satisfied that s 10(3) did require the use to be a trademark use, nor that it must be a confusing use, but was prepared to assume that it did". This comment obiter is an interesting point since the statute, new since 1994 and not well tested, only refers to ... uses in the course of trade – it does not spell out "use as a trade mark or confusing". In general, revocation of a mark through non-use is covered by Trade Mark Act 1994 s 46(1) which allows five years' grace following the date of registration and (2) where genuine use of the mark is interrupted for up to five years post-registration. The new legislation has no equivalent to TMA 1938 s 26(1) that allowed a mark less than five years registered to be attacked because there was never any bona fide intention to use it as a trademark. This omission effectively strengthens the position of anyone stockpiling marks – a point to which we shall return later.

On the basis of these opinions, His Lordship stated that threats to infringe had been established, and injunctive relief was appropriate.

AN OPTIMAL OUTCOME?

The opinion of Aldous LJ appears intuitively to make social and economic sense. Owners of trade names are entitled to a return on their investment. Purchasers of goods and services need to be assured of the quality and origin of the goods that they buy. Those who wish to free ride on the efforts of others should be deterred from doing so.

However, one of the difficulties with this intuitive approach is that it is incomplete. How are we to know, for instance, whether it is a socially or economically desirable to allocate rights in a novel variant of property to those who already hold a related and existing property right? While it might be argued that a right to use the trade name in known/accepted or usual forms of communication might

entitle the owner of the right to protection of its use in a new form, the original right itself is not unlimited. Nor is it automatically granted everywhere in new forms. Existing rights are confined for instance in terms of geography, type of business, seniority of use, and appearance, while state laws in the US often state that customers do not have proprietary rights in telephone numbers which incorporate "recognition" names (a "novel" form of right).

Other questions need to be answered. For instance, how much protection needs to be given to the owners of trade names – enough to recover the costs of informing the consumer of the quality of the product, or enough to cover these costs and make an economic profit?

Intuition cannot answer these questions. Logical analysis may, and we use the concept of economic efficiency to analyse the problem and assess the opinion. [For a full discussion and definition of property rights and economic efficiency see C W Maughan, *The Economics of Property Rights* (1995) 1 NZBLQ 78 and *Meat Competition and Efficiency: an Economist Looks at Commerce Commission Decision No 273* (1996) 2 NZBLQ 216.]

Thus, the key issue with existing trade names, whether they are affixed to buildings, printed on T-shirts, or incorporated in Internet domains, is not whether they should be protected, but to what extent they should be protected

THE ECONOMICS OF INTERNET DOMAINS: PROPERTY RIGHTS

Well-defined, universal, enforceable, and transferable property rights are essential for economic efficiency. Without them economic resources will either be overexploited due to free riding, or under-exploited in anticipation of free riding. On efficiency grounds, these rights must be transferable in order to allow the goods to move to their highest valued use, and the transfers must take place through voluntary exchange between buyer and seller in competitive markets where undistorted prices act as signals. To prevent distortion of prices, it is important that the right to exclude should not be so strong that the quantity of the good available for exchange is artificially restricted and the price artificially raised. On the other hand, if the right to exclude is too weak, users will free ride. There has to be a balancing act, so that the right to exclude is of efficient scale.

This notion of efficient scale applies to all property, including intellectual property. Thus, the key issue with existing trade names, whether they are attached to goods, used in advertising by the owner of the name or by a competitor comparing products, affixed to buildings, printed on T-shirts, or incorporated in Internet domains, is not whether they should be protected, but to what extent they should be protected. Too much protection and the cost to consumers of buying the goods will rise as a result of monopoly: too little protection and the cost of finding and verifying the quality of the goods will rise as a result of increased transaction costs.

THE ECONOMICS OF TRADE NAMES: EFFICIENT SCALE

Under the theoretical conditions of economic efficiency, information is assumed to be costless and transaction costs are assumed to be zero. Consequently trade names (and advertising) are unnecessary. Reality, however, conflicts with theory, and in the real world we observe and have to explain the existence of trade names, branding and advertising. Broadly speaking this anomaly is explained in the economic literature in one of two ways. Either the trade names are a barrier to competition designed to create super-normal profits – an anti-competitive explanation: or the trade names are a device to lower real life information and transaction costs by affirming quality and by identifying origin and point of sale of the goods – a pro-competitive explanation.

The policy implications of these explanations are that, if the names are anti-competitive then they are by definition inefficient and the property rights too strong. If the names are pro-competitive, then they are efficient up to the point where the marginal cost of creating the name is equal to the marginal benefit.

Thus, policy which is aimed solely at enhancing economic efficiency requires:

(a) that trade names are part of information markets;

(b) that the names should be used to reduce costs in information markets by signifying unambiguously the quality and origin of goods [this objective is now somewhat in conflict with the permitted practices of merchandising or trafficking in the name, and with the use of the name by competitors in advertising copy];

(c) that the names should not be used to create incontestable monopolies; and

(d) that in the long-term the owners of the names should obtain only a normal rate of return on their investment in the brand.

THE LAW AND INTERNET DOMAINS

The law, whether or not it is based consciously on economic efficiency, reflects a concern for the requirements for economic efficiency outlined above.

Schechter [quoted by Annand in *Blackstones TMA 1994*] gives four functions of the trade mark: origin, product differentiation, guarantee function, and advertising function. Origin and the guarantee function have been historically the most important; but differentiation and advertising have become more prominent with the development of mass production and with the advent of character merchandising. Under the origin and guarantee theories, the names are there to signify to the consumer that the good comes from a particular firm, and that the good has a particular bundle of characteristics (quality) which are associated with that firm. Under the advertising and differentiation explanations the names are there as symbols of the goodwill associated with the product and with the product characteristics. Under all explanations there are the ideas that each name is unique and not to be confused with any other name, and that each unique name symbolises a unique bundle of product characteristics. Hence the Courts tend to defend unique or distinctive names (strong in the USA); and frown on firms which try to copy such names.

From the point of view of the owners of trade names, it pays to choose names that are thought by the Courts to be inherently distinctive. Such names are generally arbitrary, fanciful, fabricated, or non-descriptive (Lava shoes, Diageo alcohol, Virgin trains). Names which inherently lack dis-

tinctiveness (weak names) are difficult to defend in Court. Typically, such names are those which are already in use by other firms, which are generic (PC), or which are descriptive without secondary meaning (Vision Center). However, some inherently descriptive or weak names can become distinctive with registration, long use, and advertising (eg McDonald's), while some inherently distinctive names can become weakened over time through over-use. (Kiwifruit, aspirin, and cellophane all started as distinctive names which were protected by the law, but which became weak through genericisation and so lost that protection.) The reluctance of the Courts to protect the generic and descriptive names reflects not only a desire to improve information markets, but a more general desire to prevent the monopolisation of what is common property, eg everyday language, common shapes, colours, ideas, and the like. Again this second idea is in keeping with economic efficiency.

From the point of view of those who wish to use the same name as another firm, or a similar name to another firm – for whatever reason, fraudulent or not – certain basic rules have to be followed to prevent the Courts finding them liable for passing off. The most important of these are that: strong names should generally not be copied; that choosing an identical name (identical in every way including sound, appearance of lettering, colour type of font, and so on) is more likely to be condemned by the Court as passing off than choosing a similar name (different spelling, different lettering etc); and that using a same or similar name in the same markets and for identical products as an existing user, is more likely to be viewed as infringement than choosing a similar or same name for different markets and for different products. Other rules relate to questions such as the seniority of marks, actual confusion, and the intent of infringers. Most importantly, as His Lordship noted, it is not any single one of these factors that will affect the Courts but all of the circumstances in a particular case. In other words the idea is that the Courts balance their conclusions – an idea quite consistent with efficient scale.

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EFFICIENCY, AND BALANCE IN THE OPINION

Judges in general have an unenviable task in deciding economic cases. They cannot be expected to be economists (see Epstein *Do Judges Need to Know Any Economics* [1996] NZLJ 235) but they are expected to make judgments about cases which have economic outcomes. Epstein suggests that one way in which they might do this is to be sceptical about the motives of all parties to litigation, and use simple rules of the thumb which have evolved through time, and which tend to reflect efficient principles. Had His Lordship followed Epstein's suggestion, he might well have delivered an opinion more influenced by his own comment on the need to consider "...all the circumstances..." since his opinion tended to emphasise intent almost at the expense of the other criteria. This lack of balance may lead to inefficiencies in future allocation of resources.

Consider, for instance, the two names that Aldous LJ used as examples – Virgin, and Marks and Spencer. Virgin, used as a trade name, is written in a particular style of graphics, coloured red and applied to a wide variety of products ranging from airplanes to trains, banking and vodka. It is inherently distinctive in these fields in that it is non-descriptive, in a particular script, and much advertised. Moreover it is established in several countries in diverse fields of activity. It is, however marginally weak in areas outside its core businesses since, absent the particular style of the Virgin logo, it is a commonly used word, and since it is already used in many other trade names.

The name Marks and Spencer on the other hand would not have been inherently distinctive when it was first established since it comprises two common names (initially without reputation), either or both of which might already have been used to describe existing other businesses. Its only initial claim to distinctiveness would have been the juxta-position of the two names. M&S, the initials, would have been even less distinctive, since many combinations of names and words might have led to such initials. The brand has, however, become distinctive through use and advertising and is now difficult to challenge. Moreover, since the name Marks and Spencer is not written in any particular script, and is still distinctive, it would be more potentially defensible in novel forms than Virgin.

Although Aldous LJ was aware of this distinction, His Lordship nevertheless found that both these brands and other brands had been infringed or might be infringed. With respect, this opinion can be questioned on the grounds that the full balance of factors was not adequately considered. Virgin in the lower or upper case keyboard script of an Internet domain is substantially different from Virgin when written in red and painted on aircraft and trains. Moreover, it is at least arguable that the intention of the defendants might have been to sell the name to, say, Virgin Nurseries (who did not know how to set up a domain and valued this service). Although a similar argument in relation to Marks and Spencer is more difficult to establish, there is still no inherent reason why the name should not have been established and sold to a shipyard or an engineer. The point is that no one can know the true intent of the registerer and no one can know the true intent of the plaintiff owner either. Both might have ulterior motives for registering the name – the one to free ride, the other to create or extend a monopoly. Similarly, both might have legitimate motives. Decisions made principally on the grounds of the intentions of one party, without due consideration of the intentions of the other party, and without full consideration of the implications of the balance of circumstances, run the risk of establishing world -wide incontestable monopolies in trade names – an outcome certainly not desired by the common law.

THE ASSIGNMENT OF RIGHTS

Balancing the various rules in order to achieve efficient scale is not the only issue. There is the related issue of how best to allocate rights that are in new or in novel form (technically an issue outside economics, although impinging on economic efficiency).

The present procedures for allocating novel rights are somewhat hit and miss [for a fuller discussion see Oppendahl and Larson, *New York Law Journal*, 14 Feb 1995 cited at http: www.patents.comnyljl.sht]. Regulatory authorities tend to assign the names on some rule of thumb basis that

is a mixture of preference, previous use, user pays, and first-come-first-served. Any subsequent difficulties are then sorted out in Court. Such a piecemeal approach is unlikely to be satisfactory in the longer term, and has the added disadvantage that it can reward inertia and perpetuates any monopolies that may exist.

A more effective system (and one that would lead to improvements in economic efficiency) would be to allocate the "new" names initially on a first-come-first-served basis, and then permit trading in the names. Such a procedure would allow the names to move to their highest valued use. It should not disadvantage the owners of the "old" form, even if they failed to register first, since they could buy their names in the "new" form from whomever had registered them. If they were rational, they would only pay a price below or equal to the marginal benefit of the "new" name. The payment to those who registered first (without "owning" the name) would effectively penalise inertia, reward initiative, and tax away any monopoly profits that might exist – all desirable outcomes on efficiency grounds.

The main risk with such a system is that it might lead to higher costs in information markets, due to the increased possibility of passing off. However, such a risk could be minimised by tying the concept of passing off much more closely to use, and restoring the ability to attack unused marks. Thus, those who stockpiled names without using them quickly (whether they were owners or potential infringers) would forfeit the right to use the names, while those who used the names without right would be liable for passing off. The effect of these measures would be to prevent free riding as well stockpiling. Again this outcome is desirable on efficiency grounds.

At the moment, the outcome to which we appear to be moving is not efficient. Large established name owners who have the size and resources to litigate are being rewarded with something very close to monopolies, even though they are demonstrating an inability to keep pace with new technology. Smaller established name owners are then free riding on the decisions which favour the larger players. New, potentially dynamic, players are being penalised. It is all rather reminiscent of the way in which export meat quotas used to be allocated to established firms rather than new firms, irrespective of the performance of these firms in the marketplace. Is this really the way we want to go? ❑

POSTSCRIPT AND RESPONSE

Nicholas Russell, The Law Commission

The High Court judgment in *British Telecom v One in a Million Ltd* was followed by Baragwanath J in *Oggi Advertising Ltd v McKenzie* (HC Auckland, CP 147/98, 2 June 1998). The plaintiff succeeded in obtaining an injunction preventing the defendant from using a domain name featuring the plaintiff's name and requiring the domain name to be assigned to the plaintiff. It differs from the English case to the extent that it is based on the tort of passing off rather than infringement of a trade mark; but it clearly establishes the principle that intellectual property rights are enforceable in cyberspace as elsewhere.

The question is raised, whether the enforcement of intellectual property rights in a supposedly new environment (more of that later) is economically efficient. Three comments may be made in response.

First, as Dr Maughan and Ms Soetendorp acknowledge, intellectual property rights are not necessarily justifiable in terms of economic efficiency in the first place, regardless of the medium in which they are created or infringed upon. To suggest that the application of intellectual property rights in cyberspace may be economically inefficient is therefore a truism, but one which tells us nothing whatsoever about the state of the law.

Second, and more importantly, the point should be made that simply because one transfers conduct from a physical environment to an electronic environment does not magically alter the nature of that conduct. Passing off is passing off, regardless of whether it occurs in cyberspace or elsewhere, and a representation of a trade mark may appear in any visual medium. Further, it would be impracticable to establish a rule which would render a trade mark enforceable in the physical world, but unenforceable when used as a domain name in cyberspace. What happens when the owner of the domain name wishes to advertise his or her site in another medium?

Third, the suggestion is made that the decision in *British Telecommunications plc v One in a Million Ltd* that the defendants may have had a lawful reason for registering the domain names and that these were not taken into account by the Court. With respect, this line of reasoning is difficult to understand. If I register a domain name which is similar to a trade mark for a lawful purpose, then there is no breach. The whole point of *One in a Million* and *Oggi Advertising* is that in both cases the Court found that the defendant had no intention to use the domain name for a lawful purpose. Rather, the defendants were trying to make a profit from the fact that the plaintiffs had already made substantial investments in their names and were therefore likely to pay to protect them.

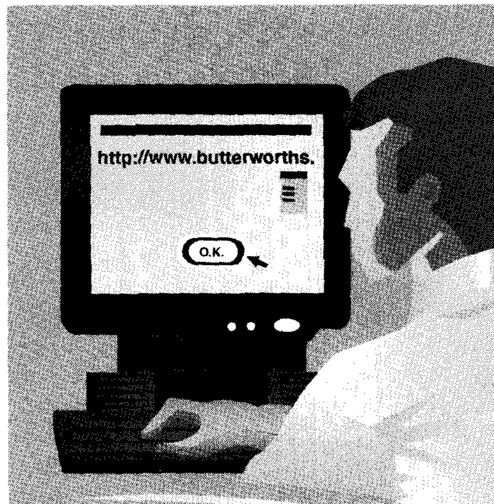
The end result of these decisions is to arrive at the unsurprising conclusion that the Internet is not a legal blank slate. Rights cannot, and should not, be undermined simply by changing the medium; this would have the inevitable effect of curtailing the right of an owner to exploit his or her intellectual property to an extent which would reduce its value. The real challenge for intellectual property law in cyberspace is the irrelevance of physical geography. The question the law must answer is, whether a New Zealand domain name infringes on a trade mark registered in, for example, Finland? The geographical distinction is irrelevant to Internet users and invisible to search engines looking for the name only. It is the global nature of the Internet which will ultimately have the greatest impact on intellectual property rights, whether this is "economically efficient" or not. ❑

THE INTERNET – A NEW WORLD WITHOUT FRONTIERS

Clive Elliott, of Baldwin Shelston Waters, Auckland

asks how the Internet is affecting concepts of jurisdiction

The Internet, a seamless network of computers, is revolutionising the way we live and do business. It is also likely to radically change the way lawyers choose a forum and how they resolve disputes in the future.



Jurisdictional questions, including choice of law, choice of forum and extraterritoriality are not new. Indeed, in international trade situations, transactions having connections with more than one jurisdiction are common.

The essential difference with the Internet is that in so-called "Cyberspace" both formal and informal relationships can be created at the speed of a single key stroke. In the space of seconds, connections can be made with one or more entities in many countries around the world. Indeed, in many cases, once a transaction or message is initiated or posted a person cannot retract the statement. The Internet is not a place to have second thoughts!

JURISDICTION

Given the diversity of regulation of the Internet from country to country, "forum shopping" will not just be advantageous but in some cases vitally necessary. The US Courts, for instance, have looked at the consequences of commercial dealing on the Internet. As stated in *California Software Inc v Reliability Research Inc* 631 F Supp 1356, 1363 (CD Cal. 1986):

> Through the use of computers, corporations can now transact business and communicate with individuals in several states simultaneously. Unlike communication by mail or telephone, messages sent through computers are available to the recipient and anyone else who may be watching. Thus, while modern technology has made nation-wide commercial transactions simpler and more feasible, even for small businesses, it must broaden correspondingly the permissible scope of jurisdiction exercisable by the Courts.

In deciding on whether a particular Court is able to exercise jurisdiction, an important question will be whether there has been sufficient contact or conduct within that jurisdiction.

The general principle is that where reliance for establishment of jurisdiction is on the basis of domicile, the Court of the state of domicile has jurisdiction to award damages in respect of the harm caused, regardless of where it occurs and not merely in respect of damage within the forum state (*Shevill v Presse Alliance* [1995] 2 AC 18). This would presumably apply in a situation where there was the commission of a tort, say for example, passing off where the harm occurred in overseas markets, beyond the immediate reach of the local Court but nevertheless was suffered by the locally domiciled plaintiff.

Take, for example, the state of New York, USA which has a "long-arm" statute that allows the state's Courts to deal with matters which come within its purview. Where:

- a non-resident/domiciliary defendant commits a tort in New York (CP LR s 302(a)(2)) or commits a tort outside New York which causes a foreseeable injury in the state; and
- the defendant derived a substantial portion of its revenue from international or interstate commerce;

the New York Courts have jurisdiction (CPLR s 302(a)(3)(ii)).

This provision relates broadly to R 219(a) of the High Court Rules. Proceedings may be served out of New Zealand without leave:

> Where any act or omission for or in respect of which damages are claimed was done or occurred in New Zealand.

A review of recent American case law indicates that there is no clear trend one way or the other. Some Courts have adopted a flexible approach and considered minimal contact within the forum to be sufficient. Others have analysed the intent of the web site operator and looked closely at where the infringement occurred. The result has been to deny jurisdiction.

Two recent cases illustrate where the boundaries might lie. The first involves a situation where a "long-arm" statute

was successfully used to reign in a non-resident defendant. In *Maritz v CyberGold ED MO* no 4:96CV01240 ERW, 19 August 1996 (available online at http://www.leepfrog.com/E-Law/Cases/Maritz_v_Cybergold.html), the defendant, a company incorporated in California, had a web site which provided details of their services, which included the maintenance of an electronic mailing list. Users would contact the defendant, which would send them advertisements relevant to the user's area of interest, accompanied by incentives to read the advertisements. Access was not limited to users from any particular country or state.

Suit was filed in Missouri. The evidence established that residents of Missouri had accessed the site on 130 occasions. It was held that the defendant's conduct amounted to either a tort committed in Missouri, or a tort committed outside of Missouri which caused injury inside Missouri. The Court held:

> Clearly CyberGold has obtained the web site for the purpose of, and in anticipation that, Internet users, searching the Internet for web sites will access CyberGold's web site and eventually sign up on CyberGold's mailing list ...

By analogy, if a Missouri resident would mail a letter to CyberGold regarding its service, CyberGold would have the option as to whether to mail information to the Missouri resident and would have to take some active measures to respond to the mail. With CyberGold's web site, CyberGold automatically and indiscriminately responds to each and every Internet user who accesses its web site (at 590).

The Court also held that the defendant, through its web site, had "consciously decided to transmit advertising information to all Internet users, knowing that such information will be transmitted globally" (at 590).

This situation seems similar to that contemplated by our High Court R 219(a).

The above is contrasted with a New York case decided at the same time. In *Bensusan v King* 937 F Supp 295; 1996 US Dist. LEXIS 13035; 40 USPQ 2D (BNA) 1519 (available online at http://www.leepfrog.com/E-Law/Cases/Bensusan_v_King.html), the New York District Court refused to exercise personal jurisdiction over a jazz club "The Blue Note" located in Missouri in a trade mark infringement action. The action was brought by a New York jazz club with the same name, which was also registered as a trade mark at the US Patent and Trademarks Office.

The defendant's web site provided information on its location, its upcoming shows and also provided a telephone number for ordering tickets. The site was even hyperlinked to the New York Blue Notes' own web site; but with a disclaimer pointing out that the clubs were unconnected. Notwithstanding this, the New York Court held that even if a user was confused about the relationship of the two clubs, any act of trade mark infringement would occur in Missouri, not New York.

This decision seems to be at odds with many others in the area. However, it is arguably "fact based" for a number of reasons. Firstly, the defendant was a locally oriented business, and was only able to provide live entertainment services in Missouri. Secondly, the plaintiff failed to provide evidence that any New York residents had accessed the web site or visited the Missouri club, as a result of having seen any advertisements or promotional materials on the web site.

In essence, it seems that the effect of *Bensusan* is that for personal jurisdiction to be exercised it needs to be shown that the non-resident defendant purposefully directed his/her Internet activities in the forum state, normally in some form of solicitation for sales and in the absence of this it is unlikely that the resident plaintiff will be able to show harm, whether economic or otherwise.

The decision has been appealed to the Second Circuit Court of Appeals (126 F 3d 25; US App LEXIS 237 42; 44 USPQ 2D (BNA) 1051). Affirming the first instance decision, the Court stressed that a New York Court may only exercise jurisdiction over a non-domiciliary who "in person or through an agent" commits a tortious act within the state. The Court said that attempting to apply established trade mark law to the fast developing world of the Internet was akin to "trying to board a moving bus". Nevertheless, the Court felt comfortable applying well-established doctrines of personal jurisdiction law to support the result reached by the District Court.

NEW ZEALAND

What is the situation if a New Zealand company wishes to sue an overseas entity which has minimum contact with New Zealand? Assuming the overseas entity has no business presence in New Zealand, the rules governing service of process out of the jurisdiction apply. The starting point is that jurisdiction is only exercised with great care and caution (*Société Générale de Paris v Dreyfus Bros* (1885) 37 Ch D 215).

Service of proceedings is allowed without leave in terms of R 219 of the High Court Rules. In the situation of a web site maintained overseas but simply accessible to New Zealand residents, generally it seems unlikely that R 219 would apply unless there are additional compelling circumstances.

In *Long Beach Holdings Ltd v Bhanabhai & Co Ltd* [1994] 2 NZLR 28, 34; (1993) 7 PRNZ 394, 400 (CA), Hardie Boys J held that it is sufficient that any part of the cause of action arises in New Zealand. This means a tortuous act itself need not have occurred within New Zealand for R 219 to apply.

Following this interpretation, if it could be established that a New Zealand resident accessed the web site in New Zealand and was misled or deceived, a relevant part of the cause of action arose in New Zealand. If, on the other hand, the only connection to New Zealand was the possible access to the web site in New Zealand, without any harm arising, no jurisdiction would appear to arise.

Proceedings may of course be served outside the jurisdiction with leave, in terms of R 220.

In terms of R 220(4) the Court, in exercising its discretion, must have regard to:

- the amount or value of the property in dispute or sought to be recovered; and
- the existence, in the place of residence of the person to be served, of a Court having jurisdiction in the matter in question; and
- the comparative cost and convenience of proceeding in New Zealand or in the place of residence of the person to be served.

A considerable body of case law exists in this area. No detailed discussion is provided, however, a few general points are made. The general principle is whether the New Zealand Court is the appropriate forum, or forum conveniens, which is another way of asking whether the interests of

justice are best served by litigating the matter in New Zealand or elsewhere.

McGechan conveniently summarises the considerations a New Zealand Court should address when deciding the issue (*McGechan on Procedure*, para HR220.05):

- It is undesirable to subject a foreigner who owes no allegiance to New Zealand to the jurisdiction of a New Zealand Court, especially where the dispute has little contact with New Zealand, or the claim is dubious;
- Whether there are proceedings in another Court;
- Whether the New Zealand Court will provide the most effective relief, or whether a foreign Court is in a better position to do so;
- Whether a party will suffer an unfair disadvantage if the New Zealand Court assumes jurisdiction.

In the situation of an overseas web site operator with no connection to New Zealand, these four factors are likely to militate against the granting of leave, absent some other factors which create a greater nexus with New Zealand. Such a nexus may however be established if New Zealand residents accessed the web site and were misled or deceived or the content somehow contravened the laws of New Zealand. This may be more likely in civil suits, eg where a New Zealand resident brings an action for the effect on their children of viewing illegal pornographic images, than in criminal suits, which are unlikely to be brought against overseas parties as a result.

The Fair Trading Act is also suitable for resolving questions as to where the misleading conduct occurred. The common law accepts that a misrepresentation can be made at one place and received or acted upon at another (*McArdle v BNZ Finance Ltd* (1990) 4 PRNZ 653).

TRANSFER OF PROCEEDINGS

The New Zealand High Court recently looked at the issue of an application under R 107 for transfer of proceedings from one Court to another, on the basis that a material part of the cause of action had not arisen in the Court in which suit was filed (*Cadbury Confectionery Ltd v The Domain Name Co Ltd*, 27 September 1996, Morris J, HC Auckland CP 398/96). The plaintiffs, in this case, claimed that the Fair Trading Act had been breached by the display of misleading material on a web site. Further there was a dispute as to whether the web site was situated in Auckland or Wellington.

The proceedings were filed in Auckland based on evidence that members of the public located in Auckland had accessed the web site. The plaintiffs argued that this established that a material part of the cause of action had arisen in Auckland, regardless of where the web site was situated. The Court accepted this, stating:

> I gather the claim involves a consideration of the Internet and the names of the plaintiffs and the possibility of their advertising their products through the Internet services. It is accepted by the defendants a person in Auckland could access the Internet and receive the information on the Internet in Auckland. The information, I am told, comes from Wellington. The causes of action pleaded involve a consideration of the actions of the person in Auckland and what the person in Auckland receives. In my view, these are material parts of the cause of action and accordingly the application fails.

Based on these considerations and the rules relating to exercise of jurisdiction in New Zealand, it is suggested that the following preliminary questions will need to be addressed:

- What market was targeted by the defendant?
- Were a specific group of people or countries expressly excluded or prevented from accessing the web site?
- Did users located in a particular country actually respond to the web site advertisement/offer to treat?

Having done this, it is suggested that the essential components for a successful attempt to establish jurisdiction will be:

- A web site;
- Conduct purposefully directed at the forum state;
- Knowledge that the plaintiff will be harmed in the forum state itself.

In summary, the likely position is that (D'Amico & Haydoutova, "Downloading the Foreign Internet Defendant into US Courts" (1997) *Cyberspace Lawyer* 2(4), 1, at p 8):

> The mere maintenance of a website, or even an electronic contract invoking the forum Court will likely not be sufficient to warrant an exercise of specific jurisdiction, but either such activity, when coupled with other efforts such as business solicitation and injury to plaintiff within the forum, will likely be sufficient to bring the nonresident Internet defendant before the Court.

Seen in this context, the question becomes a mixed one of subjective intent (what was intended by placing the advertisement on the web site) and an objective assessment of whether it succeeded (did users respond to the advertisement) thereby completing the loop. Having said this, it is likely that the intent of the web site operator will become apparent from the way he/she structures the provision of information, either by providing it to the world at large or excluding certain groups or people from specific countries.

However, in reality very few sites even attempt to exclude countries/people, and usually content is the only clue to intended audience, eg online order forms may indicate the intended respondents.

This is a complex, and evolving, area of the law. For a more detailed review of the considerations relevant in assessing whether or not a Court should exercise its jurisdiction reference should be made to specialist texts on the topic (see for example Fawcett in *Declining Jurisdiction in Private International Law* (Oxford, 1995) pp 350-358).

PROPOSALS FOR CHANGE

Various proposals have been made to coordinate an international response to "choice of law" problems in this area. Peter Bartlett, in looking at defamation, states ('Internet: The Legal Tangle' (1995) 11 *Computer Law & Practice* 110-114):

> it has been suggested that a "Cyber-Court" could be established to govern disputes on the Internet and even be incorporated into the Internet structure. Although this may provide a non-legal forum for adversaries to resolve their differences in the short term, in view of the current expansion of the Internet, this does not seem appropriate for a mainstream communications network.

In another related area, a trans-national dispute resolution body may become reality sooner rather than later. The resolution of domain name disputes has become an international problem. In 1996 the International Ad Hoc Committee (IAHC) was set up. It is a coalition of participants from

the broad Internet community. Its somewhat ambitious but commendable aim is a complete revamp of the Internet's global domain name system (DNS) (the IAHC's February 1997 and subsequent reports are available online at http://www.iahc.org). This includes the creation of seven new top level domain names (TLD's) which would reside on a shared database and a new body, a Council of Registrars (CORE) through which all new domain names would be registered.

The IAHC developed a structure for such a system, set out in a document published in February 1997 entitled the "Generic Top Level Domain Memorandum of Understanding" (gTLD-MoU) (this document and information pertaining to it and the new system are available online at http://www.gtld-mou.org). The IAHC was then disbanded. The gTLD-MoU has been widely adopted, with many signatories from around the world. It was anticipated that the seven new TLD's proposed by the IAHC and incorporated into the gTLD-MoU's framework would be released in March 1998. However, this was delayed by the release by the US Government in January 1998 of a Green Paper addressing the issue of domain names and Internet address (available online at http://www.ntia.doc/ntiahome/domain name/dnsdrft.htm. The comments made in response to the Green Paper are also available online, at http://www.ntia.doc.gov/ntiahome/domainname/130dftmail/). While some of the Green Paper proposals are in accord with those of the gTLD-MoU, there are areas of difference which mean further discussion will be needed before any action can be taken.

The gTLD-MoU has also established a procedure for resolving disputes concerning domain names. This has been developed jointly by the World Intellectual Property Organisation (WIPO) and the Policy Oversight Committee (POC) set up by the gTLD-MoU. The procedure allows an intellectual property right holder to petition a panel of international experts to determine if a domain name contravenes the domain name allocation policy. It includes on-line mediation, optional arbitration (at the option of the right holder who wishes to challenge the domain name applicant's right to hold and use the domain name) and Administrative Domain Name Challenge Panels (an overview of these procedures is available online at http://www.gtld mou.org/presentations/cg-jan22/index.htm).

These procedures will have no impact on the jurisdiction of national Courts around the world.

There is some opposition to the CORE plan, principally from the US, which argues that the Internet should not be regulated by international bodies ie it should be regulated by US interests. Accordingly, the future of the initiative is presently uncertain.

However, assuming the CORE plan is eventually implemented, given that the ability to obtain a domain name through the Council of Registrars (CORE) will be all important, and given also that all applicants will need to subscribe to the applicable policies of CORE, the effectiveness of the on-line mediation process is likely to be enhanced. Indeed, regardless of local Court rulings, effective control of disputes would seem to vest with CORE and/or WIPO.

Given the global and seamless nature of the Internet, this development is inevitable and, if kept in perspective, is likely to be positive. How the practical realities of on-line commerce and mediation affect our lives remains to be seen. Likewise, the inevitable clash between these more informal and international types of dispute resolution procedures and the older "nation state" orientated approaches also remains to be seen.

However, the trend can be seen as a positive one as the international Internet community attempts to achieve sensible self-regulation beyond the scope of any particular legal system. That is particularly so if we acknowledge that the jurisdiction of national Courts to regulate the affairs of their citizens remains largely unfettered.

IMPACT ON THE LEGAL PROFESSION

It seems, the real challenge over the next few years will be how the Courts react to forum shopping in Internet related cases. The Internet is not the first vehicle allowing businesses to offer goods or services in places they have never been and indeed may never go. Indeed, the provision of a service such as a web site is, arguably, little different from conducting an advertising campaign in more than one location or engaging in telephone or direct mail marketing, whereby goods or services are offered in countries where the firm or company has no presence. The Courts thus have a reasonably secure foundation upon which to tackle latter day "forum shoppers".

It is suggested that lawyers will be asked, with increasing frequency, to advise clients on issues of this type. New Zealand is becoming firmly embedded into the world of electronic commerce. Companies are entering into commercial arrangements on a daily basis. They will increasingly become involved in disputes, both wishing to take action against parties offshore and themselves becoming a target for attack from competitors in countries other than New Zealand.

Lawyers need to be careful for another reason. The legal profession is embracing the Internet with considerable vigour, as one commentator put it "moving from the Yellow Pages to home pages" with some speed. While the Internet does not recognise borders, ethical requirements still differ from state to state. Thus, lawyers who advertise their services and provide information/advice to people outside New Zealand could be slipping into uncertain and potentially dangerous territory.

Assume that home page material is available to clients and potential clients in the biggest of overseas markets, the USA. Some states in the USA require disclaimers on promotional and advertising material while some require clear statements designating what is and is not "advertising material". Some states have detailed record keeping requirements for advertisements, and others require submission of advertising material prior to use (see Hornsby, "Ethics Rules for Ads may cover Web sites", National Law Journal, 29 January 1996, available online as "The Ethical Boundaries of Selling Legal Services In Cyberspace" at http://www.computerbar.org/netethics/abawill.htm).

There are other potential pitfalls such as the conducting of an unauthorised practice of law in a particular state and prohibitions against solicitation. I suggest that the legal profession cannot sit back and wait for a client to get into trouble – trouble may come sooner and from more unexpected quarters.

Whichever way one looks at it, we are in for some interesting situations, the outcomes of which will depend as much on the technical parameters placed on us by the Internet environment as the legal rules which we will have to create to bring the "real time" world of the Internet into line with the sometimes "unreal" world of the law. ❑

MONEY LAUNDERING: GLOBALISATION'S ADRENALIN

James Rapley, The Serious Fraud Office, Auckland

discusses a modern challenge to legal systems worldwide

DEFINING MONEY LAUNDERING

Crime has traditionally been considered a domestic matter, a part of the life of each sovereign state with which it must cope. Criminals were almost always nationals of the sovereign state and crimes have generally been committed within its borders. The ability to regulate crimes and punish those who transgress society's rules has been, until recently, a matter fiercely guarded by each sovereign state. Money laundering, although not a new phenomenon, has become the talk of academics, law enforcement agencies and politicians. The reason appears to be because this crime has become an Organised Transnational Crime ("OTC") conducted on a massive scale by Organised Transnational Criminal Enterprises ("OTCE") (see *UN Report on the Fifth Session*, Economic and Social Council Official Records, 1996, Supp 10). In short, money laundering and those who engage in it, have gone global.

this crime has become an Organised Transnational Crime ("OTC"). In short, money laundering and those who engage in it, have gone global

Money laundering is defined by Rider and Ashe, *Money Laundering Control* (Dublin: Sweet & Maxwell, 1996, 207) variously as "the process by which the illegal origins of money are disguised, thereby hindering detection of the crime and allowing those involved to enjoy the fruits of the crime", and as "the process of concealing the origin, nature, source, and ownership of funds in order to confound law enforcement". These definitions capture the flavour of the crime. However, as legal concepts they are unsatisfactory. A definition of a crime requires precision in order to avoid confusion and ambiguity.

States around the world have adopted into their criminal codes detailed definitions of money laundering. These definitions vary, but nevertheless, conform to and maintain, a uniformity that, despite differing legal systems, language and culture, is far from coincidental, nor uncoordinated. In 1990, the Council of Europe adopted the Convention on the Laundering, Search, Seizure and Confiscation of the Proceeds from Crime ("the Strasbourg Convention"). It defined money laundering offences (art 6) as:

(a) the conversion or transfer of property, knowing that such property is proceeds, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of the predicate offence to evade the legal consequences of his actions;

(b) the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, ownership of, property, knowing that such property is proceeds; and, ...

(c) the acquisition, possession or use of property, knowing, at the time of receipt, that such property was proceeds.

However, it was the United States of America which took the lead in legislating against money laundering. Although the US had legislation capable of dealing with this type of crime in the 1970s, it was not consolidated and given specific status until the enactment of the Money Laundering Control Act 1986 ("MLCA"). The MLCA (codified at 18 USC. §§ 1956 and 1957; on 29 April 1998 a new money laundering Bill was introduced) sets out the offence of money laundering as:

> whoever knowingly uses or attempts to use the proceeds of some unlawful activity in some form of financial transaction with the intent to either promote the carrying on of a "specified" unlawful activity ("SUA") or engages in a transaction designed to disguise or conceal the nature, location, source, ownership, or control of the funds has committed a crime.

and;

> the engaging or attempt to engage in a monetary transaction involving property valued at more than $10,000 and derived from a SUA when the individual knows that the property is derived from the criminal activity.

The similarities with the Strasbourg Convention definitions are readily apparent. The US definition has been the most influential. The American definition and the decision to criminalise this activity, is part of their "War on Drugs".

New Zealand's and the United Kingdom's definitions of money laundering follow the Strasbourg Convention and generally accord with the US position. The New Zealand offence was enacted on 1 September 1995, becoming s 257A of the Crimes Act 1961. The core definitions are set out in s 257A(1), while the actual offences are found in s 257A(2) and (3) which read:

(2) ... every one is liable to imprisonment for a term not exceeding seven years who, in respect of any property that is the proceeds of a serious offence, engages in a money laundering transaction, knowing or believing that all or part of the property is the proceeds of any serious offence.

and;

(3) ... every one is liable to imprisonment for a term not exceeding five years who obtains or has in his or her possession any property (being the property that is the proceeds of a serious offence committed by another person) –

(a) With intent to engage in a money laundering transaction in respect of that property; and

(b) Knowing or believing that all or part of the property is the proceeds of any serious offence.

Section 257A (4) defines money laundering. It reads:

... a person engages in a money laundering transaction if that person –

(a) Deals with any property; or

(b) Assists any person, whether directly or indirectly, to deal with any property –

for the purpose of –

(c) Concealing that property; or

(d) Enabling another person to conceal that property.

if the Crown can prove that the accused knew that the funds derived from crime, then "by definition, transactions which would otherwise be unexceptional, assume a quite different, criminal complexion"

An accused is only guilty of a s 257A offence if he or she, knew, or believed, that all or part of the property was the proceeds of a serious offence (s 257A(2)).

The essence of money laundering is:

- Money, known to have been derived from crime, is converted from one form into another;
- Obscuring the origin of the money and its derivation;
- Repatriation of the transformed money to the criminal.

The recently reported case of *R v Liava'a* (1998) 15 CRNZ 524, a judgment on a s 347 application, is one of the first cases to briefly examine s 257A. Laurenson J stated that the purpose of s 257A, together with the Proceeds of Crimes Act 1991, was "to curb the activities of persons who chose to become involved in serious offences" (p 526). His Honour further stated that if the Crown can prove that the accused knew that the funds derived from crime, then "by definition, transactions which would otherwise be unexceptional, assume a quite different, criminal complexion" (p 526). In *Liava'a* it was held that changing NZ dollars, which the Crown alleged were the proceeds of a serious offence, to US dollars (to purchase cocaine in Hawaii) amounted to money laundering. The application for a discharge was accordingly dismissed.

As defined, the activity of money laundering is relatively simple, although the variations and methods used are not. (see Walter, *Secret Money* (London: Unwin Hyman Ltd, 1989)). It appears to be accepted that there are three phases or stages in the laundering process:

1. **Placement**, where cash enters the financial system.
2. **Layering**, where the money is involved in a number of transactions.
3. **Integration**, where the money is mixed with lawful funds or integrated back into the economy, with the appearance of legitimacy.

Money laundering is a transnational, rather than international, crime. However, given the uniformity of response from most states, that distinction is becoming a fine one. Nevertheless, it is helpful to bear this difference in mind, when considering its effect on sovereignty and globalisation.

THE INTERNATIONAL EFFECTS OF MONEY LAUNDERING

Despite money laundering being a transnational crime, its effect is global, international and wide-ranging. The UN described OTC and money laundering as a "formidable problem for the International Community", a new form of "geopolitics" and "one of the most pernicious forms of criminality of which the dimensions have yet to be fully measured and the impact fully determined". (*Report of the Secretary-General*, 4 April 1996 at p 4; UN Press Release SOC/CP/179 20 May 1996; UNCPJ Newsletter nos 30/31, Dec 1995 at p 5.) Leading jurists have offered similar predictions of gloom and peril (see *Money Laundering Control* (Dublin) Sweet & Maxwell, 1996).

As OTCE are not limited to operating within national borders, their international role has become increasing important and powerful. Money laundering and the activities of OTCE are said to "pose a serious threat worldwide in terms of national and international security, as well as political, economic, financial, and social disruptions". (Zvekic, "International Cooperation and Transnational Organised Crime" (1996) ASIL 537.)

Although quantifying the value of funds being laundered globally is difficult, estimates and statistics do illustrate the extent of the problem. The amount of money actually laundered in the banking system is estimated to be US$300 – $500 billion a year, US$50 billion of which is generated by Colombian OTCE in cocaine sales (Jayasuriya, "Counterfeit Medicines: Strategies to deal with a Commercial Crime" (1997) 5 Jnl of Financial Crime 7). This is believed to have caused a construction boom in Cali and resulted in half a million of Peru's seven million labour force to become involved in criminal drug related employment (Olmo, "The Geopolitics of Narco trafficking in Latin America" (1993) 20 Social Justice Nos 3-4,1).

Western countries are also affected. London, as with other western capitals, feels the effects in its financial markets, where it is subjected to the integration stage of the money laundering process. The distortion that this can cause to stock markets, influencing the economy as a whole, is recognised by the London Stock Exchange ("LSE") as a serious issue. (The writer was employed in the Surveillance Division of the LSE from 1995-1996.)

It is apparent that all states are affected by money laundering and OTCE. They are not, however, all affected in the same way. In developing countries, money is laundered and often moved offshore into Western countries, while in Western countries, it is integrated into the economy.

RESPONSES AND OTCE

The UN's initial response to OTCE and money laundering was through the Vienna Convention. Notably, it was the first international instrument to include money laundering as a crime, though limited to laundering the proceeds of drug related crime. It was also a milestone in its recognition that an internationally coordinated approach was necessary. Thus, it incorporated provisions concerning mutual assistance. Its importance lay in its requirement that all signatories enact money laundering offences in their own national criminal system.

However, it is in the sphere of regional bodies that the response has been the most coordinated and successful. The regional bodies who have taken the lead in addressing OTCE and money laundering include: the Council of Europe, the Financial Action Task Force ("FATF") founded by the Organisation for Economic Cooperation and Development ("OECD"), the Commonwealth Secretariat and the Organisation of American States. It is recognised that the primary driving force in combating money laundering, influencing all other initiatives, has been the FATF. The FATF was established, by the G-7 Summit in Paris in 1989, to examine ways to combat money laundering. The FATF members comprise of 26 sovereign states (including NZ) and two regional organisations. In April 1990 it issued a report containing forty recommendations. These recommendations are "designed to provide a comprehensive blueprint for action against money laundering covering the criminal justice system and law enforcement; the financial system and its regulation; and international cooperation". (See *About FATF*, FATF website www.oecd.org/fatf.)

[t]he old Wild West attitude, "shoot first and ask questions later", is alive and well in the United States law enforcement today. It is especially apparent in the "war" being vigorously waged against international drug trafficking and money laundering

The Forty Recommendations are described by the FATF as: "principles for action in this field, for countries to implement according to their particular circumstances and constitutional frameworks allowing countries a measure of flexibility rather than prescribing every detail" (*Recommendations*, p 2). The central factors are that the Recommendations instruct FATF members to:

1. "Implement fully" the Vienna Convention and implement domestic money laundering legislation;
2. Adopt confiscation and proceeds of crime legislation;
3. Implement legislation concerning each country's financial system in order to assist in the prevention, detection and prosecution of money laundering; and
4. Enter into bilateral and multilateral agreements to strengthen international cooperation.

The FATF report, when compared with instruments such as the Vienna Convention, is relatively uncontroversial. What is remarkable, and some would say has contributed to the FATF's success, is the role of the FATF, which turns the Forty Recommendations into Forty Commandments. The FATF states (*About FATF*, p 1-2) that its activities are threefold:

(i) monitoring members' progress in implementing measures to counter money laundering through a twofold process of annual self-assessment and a more detailed mutual evaluation;

(ii) reviewing money laundering trends, techniques and counter-measures and their implications for the Forty Recommendations; and

(iii) promoting the adoption and implementation of the FATF Recommendations by non-member countries.

The result has been that all members have implemented domestic laws to prohibit money laundering, which in turn effects OTCE. Those FATF members that were dilatory in complying with the Forty Recommendations were subjected to what the FATF calls political pressure. A clear example is the case of Turkey. On 19 September 1996, the FATF issued a public statement castigating this member and recorded its displeasure in its 1995 and 1996 annual reports. This pressure resulted in Turkey passing, on 19 November 1996, law No.4208 to conform with the Recommendations.

Those sovereign states that have responded to OTCE and money laundering have been influenced by the international or regional bodies. Money laundering was occasionally caught, though perhaps accidentally, by offences such as conspiracy to defraud. This was more the exception than the rule, with most states recognising the inadequacies of such laws, considering the recent internationalisation and sophistication of money laundering.

Specific legislation aimed at money laundering and OTCE, were not in place until the late 1980s when UN Conventions, the insistence of the European Council and the FATF, made states pass appropriate legislation. The US was the exception. It acted on money laundering and OTCE well before it was taken up by international and regional bodies. The United States has in fact led the international response, directing international and regional bodies, especially the FATF. It is, however, the United States' response to actual instances of money laundering and OTCE which illustrates that the US is determined to control this crime.

In NZ confiscated proceeds of crime go to the Crown. In the US, the law enforcement body that is able to identify the proceeds of crime and obtain a forfeiture order, gets to keep it. This has meant that most law enforcement agencies have a money laundering and asset forfeiture division. This has lead Kirk Munroe, a leading US and Canadian defence lawyer, to say "[t]he old Wild West attitude, 'shoot first and ask questions later', is alive and well in the United States law enforcement today. It is especially apparent in the 'war' being vigorously waged against international drug trafficking and money laundering". (See *Money Laundering Control* p 290.) As a result the MLCA was specifically designed to be broad and operate extra-territorially. Munroe provided the following example of Banque Leu (Luxembourg) SA ("Banque Leu" or "the bank") in *US v Banque Leu (Luxembourg) SA*, CR.93.0607 (NDCal). Banque Leu expanded into the South American market. This led to the opening, with cash, of a number of US dollar accounts in Luxembourg by Colombians. Throughout a one year period, over $2.3 million in the form of US cashiers cheques (which are similar to bank cheques) were deposited into those accounts. The flow of funds is important. The cashier cheques were sent from Colombia to Luxembourg and deposited. The

bank sent these cheques to their US correspondent bank, who sent them to the drawer (an American bank) where they were finally paid.

The US could prove that the $2.3 million in cashier cheques were from drug sales. It was also conceded by the US that the bank did not know this fact. Nevertheless, Banque Leu was convicted and its funds worldwide were frozen. This was achieved by the MLCA's ability to attribute criminality for wilful blindness, that is, the bank should have known the illegal source of the funds. Banque Leu pleaded guilty and agreed to forfeit $2.3 million to the US and $1 million to Luxembourg. The bank also agreed to submit to a money laundering audit by US auditors for three years and to publish money laundering guidelines. To ensure compliance the bank had to provide a $250,000 surety with a New York bank in favour of the US. This is remarkable in that Banque Leu is not regulated by the US and does not even have an office in the US.

The FATF meets in secret and members must comply with its edicts. There appears to have been little public debate as to the appropriateness of all of the Forty Recommendations to all sovereign states

SOVEREIGNTY AND GLOBALISATION

Money laundering will assist globalisation and thereby the erosion of sovereignty. This is the conclusion we are left with if we draw together earlier conclusions that:

- Money laundering is an international problem affecting every state, albeit, often differently;
- Global actors have responded to money laundering as a group, under the stewardship of the UN, US, the FATF and the European Council;
- Individual states' ability to act independently in this area has been severely curtailed.

MacCormick in "Beyond the Sovereign State" (1993) 56 MLR 2, has said that "unease about sovereignty is perhaps antediluvian". Cries that sovereignty and the concept of a sovereign state are a thing of the past litter jurisprudential literature. A number of commentators, when discussing money laundering and OTCE, identify that issues of sovereignty are in play in this area. Few however, link it one step further to its "spin-off" effects and role in globalisation. In order to strengthen our conclusion, some comment is required on the term "sovereignty".

MacCormick identifies that sovereignty is a "politico-legal concept" and that the notion of sovereignty in a political sense (as used by Rousseau, Locke and Austin) is linked to "the power of decision making", while as a legal one (as used by Dicey) the "essence is not power but normative order". (at 11.) MacCormick agrees that these political and legal concepts of sovereignty overlap. For the purposes of this paper, a sovereign state denotes "the concept of a territorial political order coupled with a legally defined position of near-absolute legislative power". (at 14.) Such a state is not subject to an external superior power. This is the key to sovereignty and has formed the corner-stone of legal and political thinking. It has also formed the backbone of primitivist theories in order to ensure a lasting global order (Bederman in 82 AJIL 2 (1988)).

This corner-stone has been shaken in the modern world with the advent of regional bodies, such as the European Union and the FATF. It is difficult to believe that France is a sovereign state when it is subject to European Council directives and legislation. The concept of a "sovereign state" has also been challenged by the fact of globalisation. The term "globalisation" itself is far from settled. Professor Jane Kelsey describes the term "globalisation" as having become "an academic buzz-word of the nineties". ("Globalisation, State and Law: Towards a 'Multi-perspectival Polity'" (1996) 14 *Law in Context* 31.) Globalisation in this context implies two distinct occurrences. "First, it suggests that political, economic and social activity is becoming worldwide in scope. And secondly, it suggests that there has been an intensification of levels of interaction and interconnectedness among states and societies which make up the international society". (Held, *Political Theory Today* (London 1991) 106.) Examples are the interdependence of "sovereign states" in the financial markets, telecommunications and media, and the inability of states to individually control problems such as AIDS, terrorism, global warming or pollution.

Equally, the complex global nature of money laundering and OTCE presents difficulties for a system governed on the basis of sovereignty. The international dimensions of the problem have been recognised by all global actors, as has the problem of jurisdiction. The actions of the FATF in relation to Turkey unequivocally demonstrates an erosion of Turkey's sovereignty. The action by the United States, in relation to forfeiture of assets, also highlights the fragility of "sovereignty".

Such responses by global actors erode a purist's concept of sovereignty and thereby assist globalisation. A review of UN reports is noteworthy for its near unanimity that there is a problem and in its response to the problem. There has been little said about the FATF's interference with sovereign states. Member states' representatives to the FATF are delegates from law enforcement bodies and civil servants. The FATF meets in secret and members must comply with its edicts. There appears to have been little public debate as to the appropriateness of all of the Forty Recommendations to all sovereign states. Even some of the less developed countries appear to have been swept up in the good cause of fighting crime, without much reflection on its appropriateness to individual cultures and national circumstances.

A recent example, close to home, appeared in *the Herald*. The 1997 President of the Criminal Bar Association and a leading defence barrister, were criticising New Zealand's Proceeds of Crime Act 1991, calling the legislation "draconian and mere revenue collecting". (*NZ Herald*, Friday, August 29, 1997 A9.) Amendments were called for by these critics. No mention was made of the reason why we have this Act. In reality, it can not be amended without taking into account our international commitments to the FATF, lest we be subjected to the wrath of the FATF.

Global actors' responses to money laundering and OTCE does encroach upon the sovereignty of individual states. The examples clearly support this proposition. The erosion of sovereignty applies to states from the North and from the South. But, it has been the states from the North who have shaped the encroachments that have transformed the Forty Recommendations into domestic legislation. ❑