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LEGAL PROFESSIONS

The New Zealand Law Society has got all it asked for, and maybe more, from the Minister of Justice.

The minister has announced a Legal Professions Bill to be introduced early in 2001. The key points are:

- a new profession of licensed conveyancers;
- the NZLS to remain as monopoly regulator;
- "lawyer", "barrister", "solicitor" and "attorney" to be protected titles;
- the reserved work to be exclusively defined;
- district law societies cease to be statutory bodies;
- restrictions on the NZLS power to regulate;
- regulations to be approved by the minister.

So there are a couple of steps forward. The decision in *Dempster v Auckland District Law Society* [1995] 1 NZLR 210, that the prohibition on acting as a solicitor applied to "work of a kind ordinarily done by a solicitor" will be overturned and the reserved work limited to conveyancing, Court appearance and signing Court papers.

Assuming that the NZLS rapidly produces new regulations (and there is no reason why it should) commercial partners in law firms will be able to depart from the regulated profession and call themselves transaction engineers or something. Firms will be able to spring up which say, handle IPOs and consist of a lawyer, an accountant, a sharebroker and a PR expert. Tax, employment and other subject areas lend themselves to an MDP niche firm approach.

There will also be a new profession of licensed conveyancers, making the proceeding in *NZLS v Registrar-General of Land*, Goddard J, HC Wellington, 31 October 2000, CP 82/00 a waste of members' compulsorily levied fees. This is a neutral step. The point of competition is not necessarily to shave the prices charged by a load of people doing the same things, but to find new ways of doing things. In real estate there will now be three defined and regulated professions instead of two, but the process of buying and selling real estate will not in any meaningful sense be liberalised.

Against that, there are some important steps backward.

The power of the NZLS will be entrenched, even its only real competitor, the Auckland District Law Society, will be stripped of its statutory powers. One hears of plans for the NZLS to contract its regulating power to district law societies or whatever replaces them, but this surely cannot include non-members.

The result then will be this: the NZLS will have the power to regulate anyone who wishes to use one of the protected titles. There will be a registration fee. If one is a non-member, one will have to pay fees which will be used by a body one has no role in electing to lobby the minister to approve regulations one may not approve of and to take actions one would not support, such as pursuing people like Mr Dempster through the Courts.

The minister's response is that the NZLS will have no power to regulate on business form, but only on personal conduct. The answer to this is already given. The NZLS will have the resources and incentive to lobby ministers and to issue public propaganda justifying the draft regulations it is putting up. No one will have much incentive to oppose them. The current proposals are themselves a testament to the NZLS power to lobby and protect its position.

This brings us to comments made by Goddard J in the *Registrar-General* case. Her Honour opined that the history showed that the regulation of conveyancing was by legislation in the public interest and not through self-interested self-regulation by lawyers. These comments seem open to question. Pure self-regulation can never achieve a closed shop, since that can only be enforced by law. Closed shops are imposed by law obtained by self-interested lobbying of lawyers who not only have vigorously resisted any liberalisation of conveyancing, but fiercely opposed the introduction of the Torrens System in the first place.

The major question in reality is what will happen to the District Law Societies. These are essentially organisations for taxing large firms for the benefit of small firms and barristers, as recent comment by Mr Chris Corry in *Council Brief* demonstrated. It can confidently be predicted that most members of the large firms will depart. The Law Society is of no benefit to them whatever.

And what of the Bar Association, the Criminal Bar Association, the Family Law Section and such entities? If the NZLS is to have power to contract regulatory powers why not to these bodies in respect of their members?

In the end this is all worth at most two cheers and is questionably worth the parliamentary time that will be devoted to it. The changes to business form could be brought about by the NZLS under the current structure. The district law societies could be rationalised by minor amendment. And nothing is apparently to be done about the Council of Legal Education or the Law Foundation, the latter's antics in particular requiring ministerial attention.

A commercial lawyer who wants to be free of the barnacles of regulations framed mainly by barristers and small town practitioners will have to exit the system altogether and abandon the use of the term lawyer. The case has been made for the profession to be governed entirely by voluntary bodies. So far, the minister has given no reason for not following this approach. We can only wait to see whether a reason is ever given. ❑

BAIN AND BEYOND

Ross Burns, Meredith Connell, Auckland

reviews Joe Karam's new book **Bain and Beyond** *(Reed Publishing)*

This is a book of two halves. In the first, and altogether more compelling half, Karam deals with the aftermath of his earlier book *David and Goliath*, the record of his investigation into the conviction of David Bain. The publication of his book led to a Police Complaints Authority investigation; to the successful defence of a defamation action brought against Karam and his publisher by two officers involved in *Bain*; a prosecution for breach of a High Court suppression order; and a number of further hearings in an attempt to overturn the conviction. Karam's services were called upon by those who saw themselves as victims of injustice. When Karam describes his earlier book as "a determined, reasoned and sustained expose" of police involvement with *Bain*, he accurately identifies two of the qualities that mark his book and his dogged involvement with the case. His initial interest in *Bain* has led to a four year immersion in the justice system during which he has maintained his unswerving belief in David Bain's innocence.

Later in his book he criticises the "nine magic tricks" of lawyers. But he himself uses precisely the advocacy techniques which he decries in others. His most compelling point is that the computer upon which the killer's message was typed was switched on prior to David Bain's arrival home and this point is thumped home vigorously. His later plea for an end to the adversary system in favour of the inquisitorial sits uncomfortably with an argument that is clearly adversarial in nature. When the second half of a book argues that the adversarial system is designed to obscure the truth, the strength of the argument is undermined by a first half which adopts the techniques, and by implication, endorses the results of that system.

The central theme of the second part of the book is the adequacy of our current system in doing justice. He proposes the adoption of the French/German model. In larger jurisdictions it has been possible to adduce substantial empirical evidence in favour of the argument that the adversarial system produces injustice. One need only consider the spate of wrongful convictions which came to light in England in the early 90s and the arbitrary imposition and execution of the death penalty in the United States to find evidence against such a system. It is more difficult in a smaller country to assemble a similar body of evidence, and by seeking to bolster his argument by questioning the convictions of Scott Watson, John Barlow and Rex Haigh, Karam's argument is weakened by being compelled to rely upon evidence which is less than compelling. If, as he claims, over one per cent of convictions in New Zealand are of innocent defendants, he should be able to find better illustrations.

The wrongful conviction of the innocent is to be guarded against with vigilance in any society which claims to be free. But why is it that the causes celebre which are taken up by members of the public almost invariably involve high profile cases? Is it because of the pressure placed upon the police to produce a conviction in such cases? In other words, are those accused of murder more likely to be wrongfully convicted than those accused of burglary? Or is it that people convicted of a high profile crime are more likely to attract the interest and sympathy of those outside the system?

In using David Dougherty as an illustration of his argument, Karam has chosen an excellent example. But has he chosen Scott Watson because he believes Watson may be innocent, or because the newsworthiness of the Sounds' murders attracted public opinion? Karam was criticised after the publication of *David and Goliath* as a publicity seeker. By bringing Watson, Barlow and Haigh into his camp he is courting the same criticism, which can only be detrimental to a rational assessment of his argument.

Karam's concerns about the adversarial system of criminal justice may be less opposed by lawyers than he believes, but the greatest flaw in his proposal is that there is no evidence that other systems are better. For those who work within the criminal justice system, any better system is welcome. Justice is not merely the concern of lawyers, Judges and police. It is the concern of the community. And while the community has determined and forthright people like Joe Karam, the justice system remains at the service of the community rather than the reverse.

In using the case of David Bain as a metaphor for the inadequacies of the criminal justice system, Karam is playing a dangerous game. His own analysis of the system is that it will behave both unethically and immorally to protect itself. By definition, if David Bain's innocence is to be used to provide evidence of the system's guilt, then the system will not permit him to be found innocent. Which, then, is now Karam's greater cause? The vindication of Bain or the damnation of the system which convicted him? Tactically, *Bain and Beyond* should have been two books, the first part designed to augment Karam's earlier book and aimed to enhance Bain's prospects of a pardon, and the second an analysis ex post facto of where the system went wrong.

But such would be the tactics of a worldly and astute campaigner. Karam claims to be neither, and it is difficult to avoid agreeing with his assessment of his own naivete. The reaction of the unworldly to stark reality is usually more extreme than that of the cynic. This is Karam's beauty and, at times, his downfall.

Innocence is a quality with which the criminal justice system is ill at ease but at the same time is the very quality which the system must recognise and safeguard. If only because innocence is the theme of the book and the motive in its writing, *Bain and Beyond* deserves our consideration and recognition. ❑

JAILHOUSE WITNESSES, SECRET WITNESSES

John Rowan QC, Wanganui

reviews the topic of the moment

The recent recantation by secret witness A in the trial *R v Watson* (the Marlborough Sounds murder trial) comes as no surprise.

What is of concern is that the police are permitted to call these people as witnesses where the very process of the Court hearing their evidence, often under the dignity of anonymity, may enhance them in the eyes of the jury and thereby give them a credence that even the most careful of warnings in summings up (as undoubtedly Heron J gave at the Scott Watson trial) does not balance.

Worse, it has also become the fashion to give notice of such witnesses very late in the piece or even during the trial.

In a trial that is balanced even small things can tip the scales in favour of the Crown. There needs to be a better mechanism for screening the evidence of jailhouse companions. The Law Commission should investigate and report.

I am not, of course, talking about crimes that occur in jail, where the only witnesses are likely to be fellow prisoners, but those cases where, for some hope of advantage, remanded or convicted prisoners give evidence against accused remanded in custody.

In this counsel's experience the calling of such witnesses is a recent phenomenon. When I commenced work as a prosecutor a little over thirty years ago no self-respecting detective would include such persons in his list of witnesses or bother to brief their evidence. The trend appears in the Law Reports from about 1990: see for example *R v Chignell* [1991] 2 NZLR 257; (1990) 6 CRNZ 103 CA (the Plumley Walker murder trial), but earlier examples include the Arthur Allan Thomas trial. A doyen of detectives told me that such witnesses are worthless. I have always thought he was right. Several recent high profile cases seem to have changed that culture. It is a move for the worse. Justice suffers.

While jurors have varying degrees of life experience to assist them in assessing whether people are telling the truth or not, they have little or no knowledge of the culture in prison or the strange symbiotic relationship that can develop between informers and the police person who runs them. Where information is proffered (some reliable, some not) and paid for in money (though usually not very much), or by way of other benefits a relationship of attachment and dependency can arise. Detectives are encouraged to cultivate informers. It is to be expected that detectives will apply a similar approach to an informer from within the prison system who comes forward with supposed evidence to support the Crown case on a high profile crime. Not surprisingly, such people are very rarely used in run of the mill cases but seem to emerge only when the stakes are high. The witness, from a starting point of obscurity, suddenly becomes very important.

Secret witnesses in particular are put in a unique position. They have officers assigned to them so that their needs are met and their problems addressed. They are protected, transported around the country, and promised a new identity. If remaining in custody their jailhouse routine is drastically altered. When the trial is over the witness is discarded, with little ongoing support. Reality (as witness A demonstrates) may set in. It is generally impossible for them to re-adjust. The ethics of their use and disposal seems to be of no moment.

For many people serving a long sentence or who have been repeatedly in prison, there is a change of outlook. They can become highly manipulative. For them the hope of advantage becomes magnified. The promise of a trip to Taihape is imagined as a new life in Townsville. If they can somehow also preserve their anonymity they know they have a licence to say anything that may assist the police.

Utilising the s 344A Crimes Act 1961 procedure, Judges carefully review evidence and are empowered to exclude confessions obtained from accused persons that are improperly obtained. If there are threats or promises by a person in authority and the confession cannot be saved by s 20 of the Evidence Act 1908 it is out. There have been rare cases, such as *R v Paiti* (1990) 6 CRNZ 591 where the evidence of a secret witness (known about for months but produced during a trial for murder) was declared inadmissible on the basis of limited probative value and considerable prejudice. However the general tendency has been to let such people give evidence and, where relevant, apply the approach prescribed by s 12C of the Evidence Act 1908. There the trial Judge is required to consider the need to instruct the jury with regard to such evidence with special caution. That is not enough. It does not dispel the cloak of temporary respectability they have been given for the Court hearing.

What can be done? If the police persist in calling these worthless witnesses we need to move urgently to a regime where the Crown has to apply early for leave before trial to call such evidence. It can then be rigorously assessed on voir dire. This was offered by the Crown in *R v Cullen* (1990) 6 CRNZ 28. A Practice Note would help. We need also to remove the protection of secrecy from jailhouse witnesses, which should put an end to this odious practice, which demeans justice and the reputation of the criminal law. ❑

NEW EMPLOYEES

Susan Hornsby, Greene Hanson, Wellington

asks whether they can go onto an existing collective contract

Can an employer rely on a new parties clause in a transitional collective employment contract ("CEC") to continue to engage new employees after 2 October 2000 on that contract? To perpetuate existing contractual arrangements for new employees appears to fly in the face of the scheme of the Employment Relations Act ("ERA"). But the ERA provides for the continuation of existing CECs and this arguably extends to new parties clauses.

The ERA does not expressly deal with this issue, and is notably light on transitional provisions. However s 243 does provide that a CEC entered into under the Employment Contracts Act ("ECA") and still in force on 2 October 2000, shall continue in force "according to its tenor".

These CECs are in effect transitional CEC's and not Collective Agreements ("CAs"). The original draft Bill provided that existing CECs would be treated as CAs for the purposes of the Act (cl 254), but this provision was dropped. Section 244 of the ERA now provides that a CEC continuing in force is to be treated as a CA only in limited circumstances (strike and lockout purposes, expiry dates, and in relation to when and how future bargaining is initiated). Section 245 provides that the grievance and disputes provisions in any transitional CEC will not apply, and the contract will be subject to the disputes regime of the ERA.

One possible construction of the ERA is that it sets out the procedures for engaging employees from 2 October 2000. In particular Part 6 provides that where there is no applicable CA, then prior to entering into an Individual Agreement (IA) the employer is bound to comply with certain procedural requirements (s 64). Section 65 prescribes what an IA must contain. Arguably, therefore, Part 6 contemplates that new employees shall be engaged exclusively on either an IA or a CA, and does not provide for any other options (eg a transitional CEC).

Nonetheless, Part 6 does not state that new employees must be employed on either an IA or a CA and arguably leaves the door open for other arrangements. Further, to allow a CEC to continue in force "according to its tenor" would seem to require that all the contract, including the new parties clause, be enforceable. The tenor of the transitional CEC is to allow new staff to join it.

This approach is consistent with the interpretation of previous Courts considering these words. In *NZ Building Trades Union v Zip Commercial Interiors Ltd* [1992] 2 ERNZ 489, the Court of Appeal had to interpret the words "according to its tenor" in s 184(4) Labour Relations Act 1987. The Court held that the substance and intent of the agreement in question should be given recognition and effect for the purposes of the LRA. Further, the Court held that to give effect to the agreement according to its tenor required recognition of what had occurred previously.

Ruapehu District Council v Northern Local Government Officers Union [1992] 2 ERNZ 276, related to the transitional provisions in the Employment Contracts Act (ECA), and the effect on redundancy agreements negotiated prior to the enactment of the legislation, but registered after. The Court held that Parliament's intention was that the ECA preserved existing industrial documents and settlements for a limited period although this would, for that period, extend a scheme of things abolished by the Act. On the facts, the Court held that there was no impediment to the 1991 agreement applying to the applicants from and after its registration on 8 August 1991, according to its tenor.

Arps v McCraken (unreported CT 104/93) turned on whether an employer who joined an industry after 15 May 1991 (the day the ECA came into force) but while an award containing a subsequent parties clause was still in force in that industry as a deemed collective contract, was bound by that deemed CEC. The Court agreed with the Employment Court in *Ruapehu* holding that the words "according to its tenor" in s 176(1) ECA should not be read down in any way. *Ruapehu* was held to be authority for the proposition that subsequent parties clauses should continue at least in part. The purpose of the relevant legislation was to create a transitional regime to preserve awards and collective agreements for their duration and treat them as CECs.

Further, in *Arps* the words "according to its tenor" were found to mean something close to "according to the exact words". The Tribunal held that the words meant that the award should continue in its entirety including the subsequent parties clause.

Whilst these cases relate to different legislation, the principles are relevant. The words "according to its tenor" have been construed as "according to the exact words", and the Courts recognised that Parliament contemplated the continuance of an existing regime, including in respect of new employees, for a limited period. Further, in *Arps*, the Tribunal observed that if Parliament intended to exclude the operation of certain provisions of a CEC, it would expressly have said so, in the same manner as it has done in the ERA for the personal grievance and dispute provisions.

Therefore, whilst the clear thrust of the law is that employees engaging on CAs must do so through union membership, it is strongly arguable this does not prevent new employees who are covered by an applicable CEC being engaged under that CEC on the basis of a new parties clause, irrespective of union membership. This appears to have been contemplated by the legislature as a transitional measure which will survive for the duration of the existing CEC.

Given that this is not expressly dealt with in the ERA it will not, however, be surprising if some employers and unions adopt a different approach. ❑

WORLD TRADE BULLETIN

Gavin McFarlane of Dechert and London Guildhall University

updates us on developments in international trade

EU-JAPAN TELECOMS DISPUTE

It makes a change to report a trade dispute involving the European Union in which the United States is not ranged on the other side of the table as its opponent. But this time Brussels has got the Japanese telecommunications industry in its sights. The main Japanese telecoms corporation is NTT, which is subject to 46 per cent government ownership. This in the eyes of the EU commission means that the current system of regulation of the domestic industry by the Japanese telecoms ministry lacks transparency, and is in effect simply a front for an effective monopoly of the industry by NTT. The specific complaint by the Europeans is that the interconnection charges which are imposed on competing companies from abroad are very much higher than they should be. In response to this criticism, Tokyo has offered to reduce NTT's interconnection charges by 22.5 per cent over a three year period, but this is said by the EU to be a derisory amount. The EU commission considers that these inflated interconnection charges allow NTT to build up very large reserves which can then be applied to the buying up of its competitors abroad. In other words the maintenance of such high rates amounts to a subsidy which is illegal under the terms of the WTO's rules. It is claimed that the playing field is not level, and that the WTO agreement on the liberalisation of telecommunication services is being breached. Under this agreement, member states must have competitive safeguards in place, and must prohibit restrictive practices such as concealed subsidies. They must permit companies which are in competition to interconnect on terms which are not discriminatory, and in particular to appoint a regulator who is not subject to the influence of any domestic supplier of telecommunications services. As a first step, the EU is asking Japan to fulfil its obligations by the appointment of an independent telecoms regulator. Tokyo has so far denied that any cross subsidisation is taking place, and that NTT has been divided into five separate trading companies in order to safeguard against this. The European commission has retorted that an absence of transparency has made it impossible for objective observers to tell whether or not subsidisation is taking place, and has served notice on the Japanese government that unless its fulfils its obligations in this area, a complaint will be lodged with the dispute resolution forum of the WTO.

WTO IMPLEMENTATION AND TRANSITION

As part of the work of preparation for a new round of GATT negotiations, the WTO secretariat is continuing to work on the outstanding concerns of the various member states which have come into prominence since the failure of the Seattle meetings in December 1999. As each new folio of agreements comes into being following the successful completion of another round of negotiations, so the question comes into play of the implementation by all member states of the obligations to which they have signed up. This has to be done against a background of complaints from WTO members in the third world that they need time to put themselves into a position where they can take on burdens which they contend are much more onerous for them than for more highly developed economies. A review mechanism has been established to consider proposals received from a number of developing states, and this is aimed at finding solutions to complaints which were aired by the third world members at the Seattle meetings. Prominent among these was a lack of consultation by the developed world, which the underdeveloped states claim were trying to railroad their own agenda through behind closed doors. The shock to the WTO which followed has probably ensured that many of these complaints have been taken on board, and there is clearly more sympathy now for the position of the underdeveloped countries. In particular, a number of requests have been received by the WTO for extensions of the five year transitional period in the TRIMs agreement (trade related investment measures), as the states concerned have complained that they are unable to accept the obligations involved in this period. Another problem area is that of Customs valuation. Many requests have been received for an extension of the five year transitional period which is available here; the WTO is giving active consideration to the question of how to deal with the large number of requests which have been received for technical assistance to meet obligations in this area. So far as third world states are concerned, the real need here is for training by officers seconded from states with technically advanced Customs services.

RECORD WTO SANCTIONS

Although the dispute between the United States and the EU over American foreign sales corporations will if carried to its conclusion involve quite astronomical figures by way of sanctions, the largest figure for sanctions so far formally approved by the WTO under its dispute resolution system relates to a case which was concluded this year between Canada and Brazil. Both states had filed complaints against each other alleging that illegal export subsidies were being paid to the regional jet aircraft manufactured by the other country. The Embraer regional jet planes made in Brazil are the largest manufactured item exported by that country, and its order book is said to be worth $20 billion. The Canadians manufacture a regional jet plane known as the Bombardier,

and there is a great deal of competition in this area, which is one of the fastest growing and most lucrative areas of the commercial airline industry. The result of the cross claims was a ruling by the WTO in favour of Canada, on the ground that while the Canadians had stopped making subsidies to their aircraft, the Brazilians had not. It had been alleged that the subsidies provided to the Embraer by Brazil were equivalent to between $2 million and $5 million per aircraft. The result is that the WTO dispute resolution body has approved sanctions totalling $1.3 billion against Brazil, as Canada will be entitled to levy $230 million annually for the next five years in higher tariffs against imports of Brazilian goods.

MUTUAL RECOGNITION AND PRODUCT SAFETY

In 1997 the United States and the EU signed up to the Mutual Recognition Agreement (MRA). Under its terms the signatories agreed to cut regulatory barriers in six key sectors which generate over $50 billion in bilateral trade. It was anticipated that this measure would produce the equivalent of a tariff reduction of between two and three per cent, which would mean a saving for US exporting companies of over $1 billion each year. The IT and telecoms industries were to be in the vanguard of this initiative, which had the widely expressed support of senior US and European executives. But the MRA has fallen foul of domestic regulatory agencies in America, which claim that the agreement has sold out US regulatory controls to foreign agencies. The agreement was due to kick in at the end of 2000 in respect of electronics, computers and telecoms equipment, but the American regulatory bodies are declining to recognise European product testing and safety standards as on a par with those applied in the USA. The philosophy behind the MRA was that products certified as safe in the territory of one signatory could be freely marketed in the territory of the other, which would give a considerable saving in time and money. Multiple certification is a nightmare for high tech industries such as IT, where large numbers of new products may be produced annually. The United States Occupational Safety and Health Administration (OSHA) is responsible for industrial safety standards, and that organisation delegates the task of safety testing to private laboratories which have met OSHA's own performance criteria. The European commission contends that the big idea behind the MRA was the transfer of responsibility for safety certification from OSHA to the national safety agencies within the member states of the EU. The result would be that a new product developed in say Portugal would be tested by the Portuguese regulatory authorities for compliance with the standards applied by the United States, and if positive certification was given by the Portuguese, that would satisfy the US requirements without further testing in the United States. The EU has complained that the current refusal of equivalence for the 15 domestic regulatory bodies within the EU will introduce a serious distortion of competition between American and European businesses. Yet another transatlantic trade dispute could be winging its way to the dispute resolution process of the WTO if an acceptable agreement is not reached between the two sides.

EU REPORT ON US TRADE BARRIERS

Each year the European commission issues its report on what it perceives as US barriers to trade and investment. It is introduced each year as being in the context of a transatlantic economic relationship, but the aim is clearly to draw attention to what the commission perceives as the obstacles which European exporters and investors meet in the United States. The report acknowledges that much progress has been made in recent years following a joint EU-US action plan which was adopted at a summit meeting in December 1995. Under the action plan, the EU according to the report had intended to give particular priority to specific initiatives in the fields of technical barriers to trade and regulatory cooperation, but as has been noted, the MRA has already thrown up serious problems. The commission additionally notes that despite the substantial reduction of tariffs which was agreed in the Uruguay round, the United States still maintains a significant amount of duties and tariffs in such areas as food products, textiles, footwear, leather goods, jewellery and costume jewellery, lorries and railway carriages. So far as information technology products are concerned the WTO agreement on that topic meant that tariffs on a wide range of IT products are to be eliminated by the end of the current year. This includes all semiconductors, computers, computer peripherals and computer parts. But although tariffs on fibre optic cables are to be eliminated under the WTO agreement, the US has maintained substantial protection in this field, and has also excluded tubes for computer monitors from this tariff elimination.

Brussels also complains about the frequently excessive invoice requirements which can be imposed in the United States in respect of certain products. These information requirements often substantially exceed normal Customs declarations and tariff procedures. Such formalities are burdensome and costly, and amount to a barrier to new entrants and to small companies. They are consequently disadvantaged when in competition with large and established suppliers. The EU considers that these are particularly disruptive in diversified high value and small quantity markets which are of particular relevance to European exporters. Thus Customs formalities for imports of textiles, clothing and footwear to the United States require the provision of particularly detailed and voluminous data, much of which the EU considers irrelevant for Customs and statistical purposes. There has also been an adverse revision of origin rules for textiles and clothing products imported into the US.

In another area of concern to the EU, attention is drawn in the report to US national security based restrictions. Brussels concedes the entitlement of sovereign nations to take measures to protect their essential national security interests, but it considers that it is in the interests of everyone that these are applied sparingly and prudently. The EU argues that restrictions to trade and investment cannot be justified on national security grounds if in reality they are essentially protectionist in nature, and are for purposes other than the protection of security interests. Section 232 of the US Trade Expansion Act of 1962 allows American industry to petition for the restriction of imports from third countries on the ground of national security, and these measures can endure for an indefinite time. Its application is not dependent on proof of any injury to US industry, nor is it framed to protect the economic welfare of any corporation. The European commission continues to voice its concern that this section gives American manufacturers an opportunity to seek protection on the ground of national security, when the reality is that it is intended to curb foreign competition. This is an area which the EU says it intends to monitor particularly closely. ❑

TAX UPDATE

Jan James & Paul Windeatt, Simpson Grierson Auckland

discuss recent cases on the Commissioner's care and management responsibilities

In *Brierley Investments Ltd v CIR* (1993) 15 NZTC 10,212 the Court of Appeal held that under the income tax legislation there was no scope for weighing and balancing management functions against collection responsibilities and that the Commissioner was obliged to assess and collect all tax due. Unlike in England, the Commissioner was not entrusted with "care and management" responsibilities giving managerial discretion in the exercise of the Commissioner's statutory powers.

In April 1995 this changed. Section 6A(2) of the Tax Administration Act 1994 (TAA) was enacted, charging the Commissioner "with the care and management of taxes covered by the Inland Revenue Acts". A new s 6A(3) required the Commissioner to collect over time the highest net revenue that is practicable within the law having regard to the resources available to the Commissioner, the importance of promoting compliance and the compliance costs incurred by taxpayers. Finally, s 6 was rewritten, requiring Inland Revenue officers to at all times use their best endeavours to protect "the integrity of the tax system", defined to include (among other things) taxpayer perceptions of that integrity, the rights of taxpayers to have their liability determined fairly, impartially, and according to law and the responsibilities of those administering the law to do so fairly, impartially and according to law.

The Court of Appeal has held that the new care and management responsibilities enable the Commissioner (as in England) to make sensible settlement decisions with taxpayers, rather than pursue the full amount of assessed tax – *Auckland Gas Co Ltd v CIR* (1999) 19 NZTC 15,027.

Although based on a UK statute, the implications of the care and management provision (and *Auckland Gas*) and its relationship to ss 6 and 6A(3) and to more specific provisions of the tax Acts are still unclear. While Inland Revenue continues to work on a draft Standard Practice Statement on care and management, three recent cases invite comment on the potential scope of the care and management responsibilities.

Ti Toki Cabarets

In *CIR v Ti Toki Cabarets (1989) Ltd* (CA 59/00, 4 September 2000) the Commissioner successfully applied to strike out judicial review proceedings brought against assessments. In part the taxpayers had claimed a legitimate expectation that the "substantive intention" of a Tax Information Bulletin (TIB) published in December 1989 on the GST implications of matrimonial property agreements would be applied to the taxpayers. Counsel for the taxpayers accepted that their insistence on the application of the TIB rather than on the law was because the former gave a better result, albeit being incorrect.

The TIB policy had been in existence for eight years at the time the taxpayers' dispute commenced and was only withdrawn three years later. The Commissioner argued that the taxpayers' case was distinguishable from the situations discussed in the TIB. The Commissioner also argued that the TIB was not binding and that the Commissioner could not be estopped from making what he thought was a correct assessment.

The High Court held that there was a tenable case for judicial review based on breach of legitimate expectation. Nicholson J referred to *Preston v IRC* [1985] 2 All ER 327 (HL) and to a statement in *Miller v CIR*; *McDougall v CIR* (1997) 18 NZTC 13,001 at 13,048 where Baragwanath J rejected the Crown's argument that Inland Revenue staff could simply ignore a policy statement on the general anti-avoidance provision as not binding:

> Whether ... it provides a fetter on their authority, or ... should be construed as giving rise to a legitimate expectation ... the result is the same: the directive must be complied with.

Nicholson J ordered, however, that the review proceedings be consolidated with separate challenge proceedings (the latter being concerned with substantive rather than procedural matters) brought by the taxpayers.

On appeal, the Commissioner argued that Nicholson J was wrong to hold that an alleged breach of a legitimate expectation can give rise to a cause of action. Counsel submitted that ss 6 and 6A of the TAA did not warrant departure from the previous New Zealand tax position in favour of the English position in *Preston*, on the basis that the care and management provisions were introduced with a clear appreciation of the statutory differences between New Zealand and England. Counsel argued that the introduction of a binding rulings regime (absent from England) at the same time as ss 6 and 6A lead to a strong inference that Parliament intended that binding rulings would be the only way in which the Commissioner may be bound by previous conduct.

The Court of Appeal decided it did not need to determine whether judicial review on the ground of denial of legitimate expectation could ever be brought in tax matters. It held that what the taxpayers sought to review was the Commissioner's ruling that the TIB did not apply. The Court regarded that as a substantive decision which

> can be, and must be, contested in the challenge proceedings and essentially on the same ground – perhaps estoppel in another guise.

Notwithstanding its dismissal of the judicial review proceedings, it appears that the Court of Appeal considers the

taxpayers can argue in the challenge proceedings that the Commissioner must apply the TIB, rather than the law.

In so limiting the taxpayers to their challenge, the Court of Appeal referred to *CIR v New Zealand Wool Board* (1999) 19 NZTC 15,476 where it said that "any scope for invoking legitimate expectation is necessarily limited by the scheme and purpose of the income tax legislation".

If the taxpayers relied upon the TIB in structuring their affairs, then the Commissioner's care and management responsibilities and the need to protect the integrity of the tax system (including taxpayer perceptions) would support an estoppel. The *Wool Board* decision (which rejected judicial review of an assessment made prior to the introduction of ss 6 and 6A) may not rule that out – albeit in challenge proceedings.

Vela Fishing

In *Vela Fishing Ltd v CIR* (M 367/98, 4 September 2000) the taxpayer filed its tax return for the 1991 income year in July 1993. At that time, s 25 of the Income Tax Act 1976 prevented the Commissioner from issuing an assessment increasing the taxpayer's liability more than four years after the end of the income year in which a return was filed. On 20 March 1998 (11 days before being time barred) the Commissioner asked the taxpayer to waive the time bar for six months after the taxpayer had asked for more time to comply with information requests. The Commissioner relied on s 108B of the TAA which, at that time, allowed a taxpayer to sign a waiver extending the time bar "applicable under ss 108 or 108A" of the TAA.

The taxpayer signed the waiver and further assessments were issued within the extended time period. Later, the taxpayer challenged the validity of the waiver and those assessments.

The High Court upheld the taxpayer's challenge, finding that the relevant time bar was in s 25 of the 1976 Act, not the time bar in the TAA that (at the time) applied only to returns filed after 1 April 1997. The judgment itself is of limited application because s 108B now expressly applies to both s 25 and the time bar in the TAA, although not to any waiver signed and delivered before 17 November 1998.

Vela Fishing appears technically correct. It does not, however, consider the question of whether, under the care and management provision, the Commissioner can depart from the strict law with the taxpayer's consent. Before the introduction of the care and management responsibilities it had been held that the Commissioner cannot waive a statutory provision, even with the taxpayer's agreement – *Reckitt & Coleman v Taxation Board of Review* [1966] NZLR 1032. Whether this now remains good law is unclear.

The Court accepted that the taxpayer and the Commissioner believed, at the time of signing, that the waiver constituted a valid legal act. The possibility of an estoppel against the taxpayer, however, on the ground that the Commissioner had a legitimate expectation that the taxpayer would not seek to renege from the waiver was not considered.

Without the waiver, the Commissioner would have issued further assessments on or before 31 March 1998. Therefore the waiver was for the taxpayer's benefit, giving it more time to persuade the Commissioner that re-assessment was not warranted. In such a situation, when reassessment could perhaps threaten the taxpayer's business, it could be a sensible pre-litigation decision, in accord with the Commissioner's care and management responsibilities, to request the waiver, even without express provision.

Case U47

Under Part IX of the TAA a "shortfall" penalty can be imposed when a tax position is taken which involves not taking reasonable care, an unacceptable interpretation, gross carelessness, a dominant purpose of avoiding tax, or evasion. Penalties range from 20 per cent to 150 per cent of the resulting tax shortfall.

The GST registered taxpayer in *Case U47* (TRA 46/99, 29 September 2000) purchased land for a taxable activity from an unregistered vendor. Under s 20(3)(a)(ia) of the GST Act, the supply of "secondhand goods" (including land) from an unregistered vendor in such circumstances entitles the purchaser to an input tax deduction equal to 1/9 of any payment made for the supply in the applicable tax period. The accountant preparing the purchaser's GST return was newly qualified. He was unaware that the vendor was unregistered and that the transaction needed to be treated as a purchase of secondhand goods. A claim was made for 1/9 of the entire purchase price, rather than just for the deposit (the balance was payable in a later taxable period). Inland Revenue queried the claim, the error was explained and a reassessment was agreed. A shortfall penalty was imposed on the basis of an unacceptable interpretation, reduced by 75 per cent to $2500 under s 141I of the TAA as it was only a temporary shortfall.

After a useful discussion of when an "interpretation" of tax law has occurred and when an agent's interpretation becomes that of the taxpayer, the TRA reluctantly confirmed the shortfall penalty. Judge Barber queried, however, "why this Accountant has been given the cane by the IRD". He noted the accountant's inexperience and the fact that Court of Appeal interpretation of a very similar provision was required. The TRA also noted that the mistiming issue only covered a period of two months (since the balance of the purchase price was paid in the next taxable period) and that Inland Revenue identified the error at the outset.

The TRA was sceptical that this type of situation was meant to be caught by the shortfall penalty provisions. Judge Barber suggested Inland Revenue had blown it out of all proportion and considered it "regrettable that an honest mistake in a specialised area of law by a newly qualified accountant has led to the might of the state creating so much stress for him ... over the sum of $2500; and this at great cost to the state".

Case U47 supports concerns expressed by the Finance and Expenditure Select Committee on Inland Revenue's application of penalty provisions in the TAA and recalls criticism levied at Inland Revenue in *Chatham Islands Enterprise Trust v CIR* [1999] 2 NZLR 388; (1999) 19 NZTC 15,075 (CA):

> The Commissioner's responsibility to collect tax ... must surely carry with it a responsibility to exercise a measure of discretion, the more so when the claim made is dubious and, when viewed in its wider context, of little or no practical utility. The Commissioner has no unqualified responsibility to try to extract every drop of possible tax irrespective of the circumstances.

In collecting tax, the Commissioner is required to have regard to the resources available. We suggest *Case U47* is an example of the Commissioner failing to exercise proper care and management and to protect the integrity of the tax system. ❑

PROFESSIONAL CONDUCT AND COSTS REVISION

Brian Keene, Barrister, Auckland

comments on Singh v ADLS

Close to the heart of every practitioner must be sound principles of professional conduct. Fee charging would come a healthy second. The two merged in a saga with apparently unfortunate outcomes for the Auckland District Law Society. Those outcomes will affect the principles to be applied by all District Law Societies in the discharge of their disciplinary and fee supervision obligations to the public and the profession.

Nicholson J in *Singh v Auckland District Law Society* [2000] 2 NZLR 604 was moved to apply s 27(1) of the New Zealand Bill of Rights Act 1990 to conclude that the ADLS was in serious breach of its obligation to observe principles of natural justice to Mr Singh's prejudice. That in carrying through (or rather not carrying through) its complaint obligations under the Law Practitioners Act 1982 the ADLS's actions were unreasonable in the *Wednesbury* sense.

Singh concerned the so-called "Intervention Rule" under which barristers are required to have an instructing solicitor and not deal directly with lay clients or have pre-payment of fees without formal account. However the principles involved apply to any professional conduct question.

It is well-known to the teams of cost revisers throughout New Zealand who work freely as a public service to review bills of costs for district societies, that cost complaints often have as their real genesis professional conduct issues and vice versa. Complainants, rightly or wrongly, believe that a failure in professional standards has adversely affected the outcome of the retainer. Cost review and professional misconduct become unfortunately interlinked.

In brief, Mr Singh, having been convicted in the District Court of theft by failing to account, filed his own Notice on Appeal in August of 1995. Some two months later he directly approached a barrister sole to represent him on the appeal. Fees in three instalments totalling $7062.50 were paid without fee accounts being rendered. The cheques were directed to the barrister. The retainer did not prosper and two days before the appeal hearing Mr Singh picked up his documents. The fate of this appeal is unknown.

Two and a half months after the appeal (August 1966) he complained to the ADLS. The ADLS regarded his complaint as being primarily directed at professional misconduct. An exchange of correspondence clarified that a full cost revision was sought. By the time Mr Singh had provided the ADLS with what it regarded as sufficient information to start upon the revision the six month period under the Law Practitioners Act for revision as of right had expired.

The ADLS, believing this to be the proper course, referred Mr Singh to s 146 Law Practitioners Act. It invited him to apply to the Court for an order allowing a fee revision on account of special circumstances. There was protracted correspondence between Mr Singh, the ADLS and the barrister during which the ADLS allowed the barrister over a month to provide a full explanation on the misconduct complaint (which directly touched upon the cost complaint). It stipulated that Mr Singh had to respond within 14 days to the barrister's explanation. In fact, he was granted a series of extensions spanning some ten months before he finally gave his response to the ADLS in February 1998. Possibly coincidentally, that same month Cartwright J made an order allowing Mr Singh's costs to be revised. Her Honour reasoned that no bills of cost had been rendered and there were two payments made within the 12 month period within which the Society had a discretion to review costs.

The ADLS promptly appointed a costs reviser and advised Mr Singh that it would deal with the professional misconduct complaint following the decision of the costs reviser. No doubt in doing so it believed that an answer to the costs question might assuage Mr Singh's other complaints. But by mischance enshrined in Murphy's Law the Society received a detailed breakdown of the bill of costs from the barrister, but failed to send a copy to Mr Singh. It notified Mr Singh in writing of a cost revision date, but sent it to the wrong address. Mr Singh did not attend and was then advised in writing by the Society that on an adjourned date it would proceed in his absence. Mr Singh protested the reason for his non-appearance was the failure of the ADLS to get his address right, despite earlier reminders of a change of address. He again asked for all documents justifying the costs. These were not provided until during the cost revision hearing which was adjourned a short time to allow him to consider the information. The ADLS reviser ruled the $7062.50 fee to be fair and reasonable.

Mr Singh appealed to the Registrar of the High Court. After cataloguing the errors of the barrister in both receipt of the money and failure to provide adequate bills the Registrar reduced the account by $2500.

Meanwhile the professional misconduct complaint was referred to a senior practitioner who was a member of the ADLS Council. His conclusions were:

- prima facie there was a breach of the intervention rule;
- the barrister needed to explain the scale of the charge. Disarmingly he concluded: "I could, having had to read all this crap, produce something like what she produced in four hours maximum: it is an overcharge as I see it".

The senior practitioner was later supplied by the barrister with a detailed breakdown of costs and an explanation about her disengagement from the brief. His conclusion was that the barrister's work was timely and diligent. He was

also satisfied by her explanation that the money she received was paid into the trust account of her instructing solicitor (but did not check on this).

As a result, Mr Singh was advised in writing that there was insufficient evidence of misconduct to warrant further inquiry or disciplinary action. The difference between his version of events and the barrister's was noted. The letter unfortunately concluded:

> It is beyond the jurisdiction of the Complaints Committee to make a determination where there is a dispute as to the facts. As you will be aware, the Court is the proper forum to make such a determination.

Five months later Mr Singh took review proceedings in the High Court. He was no doubt emboldened by the Registrar's reversal of the ADLS's earlier decision.

The ADLS swore a list of documents which claimed privilege for the confidential reports from members of the Committee and staff to the Complaints Committee. Mr Singh applied to the Court for production of such reports. The ADLS responded that the documents were not relevant to the proceedings. Wisely the ADLS later withdrew from that position. Hence came into Mr Singh's hands the memoranda quoted above which so aided his case. Thus even before trial the ADLS had suffered its first setback, namely all of the documentary material which complaints processes spawn will be relevant and prima facie available to the determined disaffected client.

A better basis for resisting discovery must lie in the general discretion which the Court may exercise in ordering production of such material. In particular, in a disciplinary proceeding, a complainant is not necessarily entitled to have access to all material relevant to the Tribunal. So the ADLS may have been right in the conclusion which it argued for but wrong in the reasoning it employed. Since complaints can be made by any member of the public, documents provided by the practitioner to the Society must be preserved from discovery. Aside even from sensitive issues such as legal professional privilege (when the complainant is not the client) there must be a public interest in preserving the openness of supply of information to the Society to allow unjustified complaints to be disposed of without releasing to a complainant information in the Society's hands.

Furthermore the nature of steps taken prior to disciplinary charges being laid or rejected is inquisitorial not quasi-judicial. The Privy Council in *Public Disclosure Commission v Isaacs* [1988] 1 WLR 1043 made it clear that a complainant in such processes had no right to receive documents or be more generally involved. The essentially adversarial practice of document disclosure has no place in being engrafted upon the duty of the Law Society to inquire under s 101. A similar conclusion to *Isaacs* was reached in *ADLS v O* (HC Auckland, 27 April 1995).

Passing now to the judgment itself Nicholson J firstly held that s 27 of the Bill of Rights Act requiring observance of the principles of natural justice applied to the revision procedure. In particular the failure of the Society to give Mr Singh a copy of the barrister's four page detailed explanation of costing was a serious breach of these principles.

Secondly he held that *Wednesbury* unreasonableness, accepted as being the stringent test of a decision "outside the limits of reason", had tainted the ADLS's approach to the disposal of the complaint. In particular, s 101 of the Law Practitioners Act requires that every complaint referred to a District Council "shall be inquired into as soon as practicable". The ADLS had castrated the system of investigation by ruling that a dispute of facts had to be determined by the Court. This, in the learned Judge's view, "would ... reduce the role of district societies ... to that of a watchdog without bark and bite". Nicholson J's approach may well have been influenced by his view that, on the sensitive question of receipt of moneys from a lay client direct, the barrister's answer was patently inadequate and evasive. On these dual grounds *Wednesbury* unreasonableness was upheld.

So the message for district societies is clearly that their statutory function requires a proper and principled determination of disputes of evidence between practitioner and client. That said, this conclusion and the weight attaching to it must be affected by *Isaacs* and *ADLS v O* which do not appear to have been cited.

Thirdly in exercising the overall discretion to intervene, the public policy consideration of upholding the standards of investigations of complaints by district societies must be rigorously preserved. At stake is the confidence which the public and the Court can place in such investigations. Such principles must be paramount. Any appearance of the Law Society "protecting its own" must be avoided at all costs.

No doubt District Law Societies will generally endorse such a principle but against the background of an inquisitorial rather than judicial or quasi-judicial process.

The final point is that even an organisation as public spirited and well meaning as a local District Law Society is amenable to a costs order when it has gone plainly wrong. Nicholson J held this was such a case. The ADLS was ordered to pay costs. These were not fixed but were subsequently disclosed by the ADLS to be agreed at $3200.

Here again the decision may be questioned. An order for costs is normally appropriate only when a party is represented by counsel. Mr Singh appeared in person. Mr Singh may be a person entitled to apply for a practising certificate but probably did not have one at the time. In fairness to the Judge this point was not argued and the level of costs was agreed.

The ADLS has since issued a commentary on the decision in the 20 October 2000 issue of *Northern Law News*. It seems likely there will be a closer review of correspondence and memoranda associated with fee and/or misconduct complaints. The strength of language used in such memoranda may well be toned down. Certainly any writer may well be more circumspect if he or she might be quoted in the *Law Reports*. Next it is likely that the complaints procedure will involve more attention to detail of disputed facts. Salutary though this may be, all lawyers will recognise the potentially onerous costs ramifications.

If this judgment represents the legal position, what is a District Law Society to do with its next misconduct complaint? It must form a view on any disputed evidential matter. It must comply with s 27 of the Bill of Rights. Natural justice in the context of the judgment is but a hair's breadth away from a hearing of some sort. In all but the most clear cut of cases a procedure akin to a disciplinary procedure/investigation may need to be instigated. Again the cost and resource ramifications of this need to be thought through.

For the bigger and better resourced District Law Societies such as Auckland these issues, although tiresome and potentially troublesome, can nonetheless be managed. For smaller societies they are likely to be yet another blow against local autonomy, forcing otherwise unwanted amalgamation. Whether this is to the good of the profession and the public it serves will be a rich field for debate. ❑

E-TRANSACTIONS BILL

Steve Keall, Chapman Tripp, Auckland

has some urgent suggestions about the proposed regime

The Ministry of Economic Development (MED) recently tabled an "Electronic Transactions Bill" (the Bill). The ostensible purposes of the Bill are to:

- remove certain legislative impediments currently preventing the use of electronic technology for communications and record-keeping in some areas; and
- remove avoidable uncertainty surrounding the legal status of electronic communications and related uses of modern technology.

In the spirit of Closer Economic Relations it borrows significantly from Australia's recently enacted Electronic Transactions Act 1999 (Cth). In this article I argue that the need for certainty in electronic transactions would be better served by following the United Kingdom's Electronic Communications Act 2000. There is a good argument that the Bill in its present form could be substantially improved by enlarging its scope. At present it only applies to statutory requirements as to form. In this article I suggest that it should also capture voluntary obligations. The UK Act also establishes the basis for a digital signature infrastructure.

Improving certainty

Part 2 of the Bill relates to "improving certainty in relation to electronic information and electronic communications". Clause 8 provides that information is not denied legal effect solely because it is in electronic form or is communicated by electronic means. I would be surprised if this proposition were not already true as a matter of general principle. However, it is helpful to have it positively stated in a statute to put the position beyond doubt.

Default rules for dispatch and receipt

Clauses 9-13 in Part 2 of the Bill provide "default rules" about the dispatch and receipt of electronic communications in respect of time and place. The default rules will interest lawyers who have been required to consider whether or not the postal rule or the rule in *Brinkibon Ltd v Stahag Stahl und Stahlwarenhandels GmbH* [1980] 2 Lloyd's Rep 556 (CA) applies to e-mail. By cl 9 the default rules will not apply where the parties otherwise agree, or an enactment provides otherwise.

Clause 10 provides that the time of dispatch shall be the time the electronic communication "first enters an information system outside the control of the originator". This will often be satisfied the moment a user hits the "send" button in his or her e-mail software. In most cases an information system will be a server, or equivalent.

Clause 11 provides that the time of receipt is the time an electronic communication enters the information system of an addressee who has designated that system for the purpose of receiving electronic communications.

As I understand this rule, a practical example would be where person A sends person B a contractual offer by e-mail, and person B accepts the offer by e-mail. The time of the formation of the contract would be the time the acceptance from person B entered person A's mail server. A reasonable assumption in this case would be that if person A communicates to person B using a particular mode, person A has consented to person B's use of the same mode to respond.

Clause 11 provides that in all other cases the time of receipt will be the time "the electronic communication comes to the attention of the addressee". There is an issue as to whether this rule includes the time the message ought to have come to the attention of the addressee.

Clause 12 provides that the place of dispatch on an electronic communication is the place of business, or, if there is no place of business, the originator's ordinary place of residence and provides more or less the same rule in respect of receipt. It is uncertain how these rules will apply to people sending e-mail remotely while away from their business or home – from overseas, for example. Possibly the intention is that the default rules would not apply.

E-mail is currently the most ubiquitous form of electronic communication. However, the default rules may also apply to other novel forms of electronic communication, such as ICQ or Internet telephony.

Writing and signatures

The preamble to the Bill states that Part 3 allows certain legal requirements to be met by using "functionally equivalent electronic technology". Those requirements include, amongst others, the need for certain information be in writing and that information be signed.

In respect of the writing requirement, cl 18 states:

> A legal requirement that information be in writing is met by information that is in electronic form if the information is readily accessible so as to be usable for subsequent reference.

In terms of signatures, cl 22 states that a legal requirement for a signature is met by means of an electronic signature if the electronic signature:

(a) adequately identifies the signatory and adequately indicates the signatory's approval of the information to which the signature relates; and

(b) is as reliable as is appropriate given the purpose for which, and the circumstances in which, the signature is required.

These definitions are reasonably uncontroversial. They copy the UNCITRAL Model Law 1996 which is deliberately general. There is a danger that they are so general they do not offer sufficient guidance about what technology will actually be "adequate" or "reliable".

CRITICISM OF THE BILL

Part 3 only touches on situations where there is a statutory requirement as to form. Voluntary obligations are left to the common law. While drafting the Bill the MED stated:

> Signatures may be relevant to questions such attribution of a message to its sender, or proving that an agreement has been entered into. In this situation there is no legal barrier to use of electronic technology for such purposes the Courts will apply the relevant principles relating to attribution, contract formation, etc.

It is submitted that this approach is not optimal. While signatures are not generally necessary for contracts, they are a typical feature – particularly in business dealings. I assume it is business the drafters desire to promote.

If we accept that the purpose of the bill is justified – to provide certainty in electronic commerce – then it is inconsistent to lay down rules for statutory requirements on the one hand and then say that contracts and other voluntary obligations should be left to the rules of evidence on the other. There has never been a legal obstacle in either case. There has been, however, an understandable reluctance to be the "test-case".

The reason the clauses about what may be a "writing" and a "signature" are included in the Bill is not to create new law, or even change the law, but affirm the true position. The object is to make the law certain. Certainty in this context means being reasonably sure about what the law is in advance, without the need to test a proposition before a Judge. Certainty should be provided across the whole legal landscape. For the time being, the position in relation to contracts shall remain uncertain.

It seems sensible to follow the object through to its logical conclusion. If common sense prevails, the Bill may be amended in the House to incorporate the view that the Act should apply to all electronic transactions generally. Otherwise, the risk is that the eventual Act will only apply to the filing of sundry Companies Office documents. Law clerks will continue their lonely vigil by the fax machine, waiting for the physically signed contract to come through-while the computer sits dormant.

Exceptions to the Bill

The Bill does not affect the following (amongst others):

- bills of lading;
- negotiable instruments, such as cheques;
- affidavits, and other documents given on oath;
- powers of attorney;
- land transfer documents; or
- rules of Court procedure, such as the High Court Rules 1992.

Most common transactions not affected

At first blush, the most significant and common transactions, and therefore those that could profit the most through reduced transactional costs, are excluded. It might have been helpful, for the avoidance of doubt, to include a list of statutes that will be affected by the Bill. By deducting the long list of Acts not affected by the Bill from the total pool of statutes, it appears that the Act should affect the Property Law Act 1956, and its formal requirements for the disposition of an interest in land or subsisting equitable interest under s 49A. It should also affect the miscellany of formal requirements under the Companies Act 1993. One such requirement is the need for a person wishing to be the director of a company to sign a consent to be a director.

THE UK ACT

The approach taken by the United Kingdom in its Electronic Transactions Act 2000 is much more forward-looking.

Section 7 states that an electronic signature:

> shall be admissible in evidence in relation to any question as to the authenticity of the communication or data or as to the integrity of the communication or data.

An electronic signature is defined as:

> so much of anything in electronic form as:
>
> (a) is incorporated into or otherwise logically associated with any electronic communication or electronic data; and
>
> (b) purports to be so incorporated or associated for the purpose of being used in establishing the authenticity of the communication or data, the integrity of the communication or data, or both.

The UK Act states the law in respect of electronic signatures as a rule of evidence. By stating the law as a matter of evidence, a fortiori all requirements as to the form of documents are captured. This approach is better because uncertainty to date has not been about whether an electronic signature is a signature or not. Rather, the heart of the matter is really the extent to which such a process is admissible in evidence. The UK Act appears to answer this question. The New Zealand Bill does not. Possibly this will be accounted for in the proposed Evidence Code. If it is, then that is a good reason to enact both statutes at the same time.

A significant aspect of the UK Act is its provision for a voluntary register of Cryptography Service Providers. For the time being at least, the best electronic signature technology is so-called "cryptographic processing". It is also known as a Public Key Infrastructure (PKI).

It is generally acknowledged in technology literature that PKI technology can only flourish if trusted third parties, also known as "Certification Authorities" (CAs) independently verify the authenticity of encrypted signatures. For more information on this subject refer to the American Bar Association's "Digital Signature Guidelines Tutorial" (http://www.abanet.org). The credentials of the CA are integral to the successful creation of an effective cryptographic digital signature framework. On this basis the UK Act provides for the creation of a public register of approved "Cryptography Service Providers".

While the involvement of a CA is not necessary under s 7 to show an electronic signature is a signature, it will be helpful. The fact that the involvement of a CA is not necessary to s 7 should go some way to alleviating worries about preserving so-called "technological neutrality". The Law Commission papers, a MED discussion paper and the Bill itself go to some lengths to suggest the rules should not favour any particular technology. Otherwise, it is argued, innovation and investment in other technologies may be discouraged. That is a legitimate concern. However, it is unlikely that any new technology is likely to be created in New Zealand, so it is doubtful whether there would be anything to discourage. So it is difficult to see technological neutrality as a real concern for our legislation.

Possibly the UK Act achieves an effective middle ground between kick-starting technology and giving an unfair advantage to a certain form of technology by acknowledging that encryption is sufficient, but not necessary. It is submitted that New Zealand should adopt the same approach. ❑

"HARLEY COSTS": A NOTE OF CAUTION

Duncan Webb, Victoria University of Wellington

finds a disturbing new practice in operation

Lawyers are adept at creating and marshalling novel procedures to gain an advantage in litigation. In some cases this entails using procedures intended for one purpose to achieve another. One ill that has been associated with litigation in the United States is the tactical use of applications against lawyers involved in a proceeding. Such applications not only impose the usual burdens of responding on the other side, but they may also drive a wedge between lawyer and client with the ultimate possibility that the lawyer may no longer be able to act. It is widely accepted that "the Court has also to be alert to tactical objections made for an ulterior purpose" (per Blanchard J in *Russell McVeagh v Tower Corp* [1998] 3 NZLR 641, 676 regarding the duty of confidence to former clients).

One such application is that of costs against lawyers personally for serious dereliction of duty to the Court which recently came to prominence in *Harley v McDonald* [1999] 3 NZLR 545. In that case a barrister and her instructing solicitor were ordered personally to contribute to the costs of the litigant against whom they were acting. The order was made on the basis that the case was so hopeless, and not supported by clear instructions from the client that it demonstrated a serious dereliction of the duty of the barrister and the solicitor of their respective duties to the Court.

There are numerous motivations for making such an application. Lawyers are occasionally frustrated by what they perceive to be the lack of competence of opposing counsel and the increased time, attention and costs which must therefore be devoted to the matter. They may form the view that the course of conduct of opposing counsel is in the interest of none of the litigants, including that counsel's own client. In such a case it may be appropriate to seek costs from the lawyer in question rather than the client.

Such an application, or threat of application might also be used as a device to create problems for opposing counsel. If made, counsel will have to inform the client of the fact that they have been accused of misconducting the client's case. If there are grounds for the application then it would, at least prima facie, appear that there is a conflict between counsel and client which would preclude the counsel from acting further. At a less invidious level, threats of such applications may be made as a standover tactic to discourage lawyers from energetically pursuing novel arguments, or seeking to pursue cases which have a thin evidential basis.

ENGLISH EXPERIENCE

These are problems which the Courts in England have already had to face with the statutory equivalent of *Harley* orders – wasted costs awards. It is suggested that the stringent requirements which the English Courts have imposed ought to be applied to the equivalent orders in New Zealand.

Applications made at conclusion of substantive matters

The Courts have been clear that, except where compelling reasons show otherwise, applications should be made only after trial: "speaking generally we agree that in the ordinary way applications for wasted costs are best left until after the end of the trial" (*Ridehalgh v Horsefield* [1994] Ch 205, 237).

The reasons for taking such an approach were discussed in *Filmlab Systems International Ltd v Pennington* [1994] 4 All ER 673. First, it will often be necessary to wait until after the conclusion of trial to see whether steps taken in the proceeding were warranted, or were steps which a reasonable barrister might have taken:

> What may seem to be a misconceived application could, after trial, be seen as an application which was worth trying as it would have saved considerable time and money if it had succeeded. It is therefore unlikely that applications for wasted costs orders will succeed in civil litigation until after the case has been completed. It is only at that time can the conduct of the legal representatives be assessed in a correct context.

Second, the effect of the application may be that the litigants are deprived of counsel of first choice. Such an application prior to the close of proceedings may infect the solicitor client relationship with a conflict of interest which will necessarily have adverse affects. This is to be avoided. In the words of Donaldson MR in *Orchard v SE Electricity* [1987] 1 All ER 95, 104:

> Whilst there can be no objection to an application [under the wasted costs provisions] at the conclusion of a hearing, given appropriate facts, it is quite another matter where such an application is threatened during or prior to the hearing. Objectivity is a vital requirement of professional advisers ... Threats to apply on the basis that the proceedings must fail not only make the solicitor something in the nature of a co-defendant, but they may well, and rightly, make him all the more determined not to abandon his client, thereby losing a measure of objectivity.

It will only be in the clearest of cases where such an application is appropriate prior to the conclusion of a case. The only reported instance of a successful application at an interlocutory point is that of *Kelly v South Manchester Health Authority* [1997] 3 All ER 274. In that case it was held that it was appropriate to make a wasted costs order against the Legal Aid Board (which was not a party to the proceedings) where dilatory conduct had led to an adjournment after trial had been commenced.

Harley applications may be an abuse of process

The Courts should be alert to the fact that orders of this kind may be applied for in an effort to attack or harass the lawyers of a litigant. Where such applications are used to harass or "browbeat" legal advisers "such conduct might be contempt of Court" (*Orchard v SE Electricity* [1987] 1 All ER 95, 106 per Dillon LJ). Indeed it is well-established that to use an application to the Court for any purpose collateral to that for which it is intended is an abuse of process of the Court and may well be a serious dereliction of the duty to the Court in itself.

Summary procedure and natural justice

While the Courts have not set out clear guidance as to the manner in which applications of this kind ought to be made they have been clear on two points. First, the application is summary in nature. Secondly the procedure must be fair.

This will mean that the lawyer against whom allegations are made must have fair notice of the application, and that the application must particularise the wrongs which are alleged to amount to serious misconduct. The words of Bingham MR in *Ridehalgh v Horsefield* [1994] 3 All ER 848 at 867, are instructive:

> The overriding requirements are that any procedure must be fair and that it must be as simple and summary as fairness permits. Fairness requires that any respondent lawyer should be very clearly told what he is said to have done wrong and what is claimed. But the requirement of simplicity and summariness means that elaborate pleadings should in general be avoided.

The Master of the Rolls continued to observe that in such a proceeding no interlocutories such as discovery or interrogatories would be appropriate, that hearings should be brief, and "Judges ... must be astute to control what threatens to become a new and costly form of satellite litigation".

The danger if such an approach is not taken is that lawyers who have acted in good faith and discharging their duty to the Court will be put to considerable expense and anxiety at the hands of a strategic device of the opposing lawyers. Moreover the very wrong which such orders are intended to avert – the wasteful and fruitless use of Court time and needless expense for other litigants – may be compounded.

Any party may make an application for a *Harley* order, or the application may be made by the Court, though the latter will be rare. However, any such application must be made on notice in order that the lawyer in question will have a fair opportunity to respond to the allegations including, if desired, instructing counsel to appear on his or her behalf. Where notice of the application is not given any award of costs will be per incuriam *Stephens v Stephens* [1991] 1 NZLR 633, 638.

Court has discretion to hear application

The making of a *Harley* order is an exercise of the Court's inherent jurisdiction to govern the conduct of and discipline those who appear before it. As such it is subject to a wide degree of discretion. The Court has an initial discretion whether or not to hear an application for such an order. Not only must there be a strong case that the order will ultimately be made, but it will also be relevant whether or not the hearing of the application will serve the purposes of the order:

> The costs of the inquiry as compared with the costs claimed will always be one relevant consideration. This is a discretion, like any other, to be exercised judicially, but Judges may not infrequently decide that further proceedings are not likely to be justified *(Royal Institution of Chartered Surveyors v Fryer* Court of Appeal (E & W) 30 March 2000, *The Times* 16 May 2000).

Court is reluctant to make orders

There is a high onus on an applicant for such a costs order to show that it is warranted. In the first place such orders are of a disciplinary nature and an allegation of professional misconduct may need to be proven to a degree greater than a mere balance of probabilities. This is particularly so where the allegations made suggest moral turpitude: *Re a Solicitor* [1992] 2 All ER 335.

The second reason for such reluctance is the Draconian nature of the order. Such an order by definition places onerous penalties on the lawyer in question. It is intended to be punitive as well as compensatory in nature and therefore should not be made except in the clearest of cases: *R v Beynon* (unreported) Court of Appeal (E & W) 29 April 1999 per Waller LJ.

A third reason is the procedural restraints on the lawyer replying to the allegations. The procedure is necessarily summary and evidence will usually be restricted to the record of the Court and affidavits. There may be constraints on the lawyers regarding the evidence which may be given to the Court due to the privilege of documents: *Tolstoy-Miloslavsky v Lord Aldington* [1996] 2 All ER 556.

A further reason for such reluctance is to discourage the making of such applications except where such an order is clearly justified. The negative aspects of such an application such as the manufacturing of further litigation, the disruption of lawyer – client relationships, and the suppression of advocate zeal dictate that they should be restricted to truly egregious conduct.

THE THREE STAGE TEST

Under the English wasted costs jurisdiction the Courts have adopted a three-stage test for determining whether an order of costs against the lawyer should be made. That test might usefully be adopted in New Zealand. Once the Court has resolved to hear an application it must address the issue of whether the duty has been breached. Second the Court must determine whether the breach has caused additional costs to the opposing litigant. Third, the Court must determine whether it ought to exercise it discretion to make such an order or whether there are reasons why such an order might not be appropriate.

Serious dereliction of duty

Costs will be awarded against legal advisers only where it can be shown that they have been guilty of serious dereliction of their duty to the Court. (*Harley* para 55.) It is not necessary that any intentional wrongdoing be shown. Incompetence of a sufficiently gross kind will be enough:

> Negligence or incompetence on the part of a barrister or a solicitor at an appropriately high level is capable of amounting to a serious dereliction of duty to the Court. While simple negligence or errors of judgment have generally never sufficed for a serious dereliction of duty, neither has it been necessary to go as far as demonstrating bad faith or other moral wrongdoing (para 57).

It is important to note that the English cases rely on statutory provisions which use the somewhat lower test of "improper, unreasonable or negligent" conduct, rather than "serious dereliction of duty". While the kind of actions which are relevant will be the same, the degree of negligence must be gross in New Zealand (*Harley* para 55), while in England mere negligence will suffice.

It is also well-established that the urgency and complexity of the proceedings in question will be relevant to whether there was a breach of the duty to the Court (*Ridehalgh*). Justice Ipp has, extra-judicially observed in respect of ex parte applications: that although the duties on lawyers are high:

> There are practical difficulties in complying with this rule to the letter. Usually instructions are received very shortly before the application is made, and often, despite the best efforts of the plaintiff and his lawyers, some relevant facts are not discovered, and therefore not disclosed. In such circumstances it is doubtful that the lawyers will be regarded as having breached their duty to the Court and that the interim injunction will be discharged merely on the ground of non-disclosure. ("Lawyers' Duties to the Court" 114 (1998) LQR 63, 69.)

It is clear that the Courts will take into account the nature of the work when considering such an order. It is clear that "allowance should be made for the fact that an advocate has to make decisions quickly and under pressure" (*R v Beynon*). The fact that the practitioner in question was diligent in taking all of the steps that could be reasonably expected in regard to the proceeding will mean that he or she acted competently, even if mistakenly: *Ridehalgh v Horsefield* [1994] Ch 205, 264. Similarly the fact that the Court has the benefit of hindsight should not affect the way in which the actions of the lawyer are judged.

Guidance is to be gained from the level at which professional disciplinary proceedings might be invoked:

> It can be said, however, that the levels [of serious dereliction of duty and professional misconduct] will often coincide, and incompetence or negligence falling short of a disciplinary level under the Act, will not ordinarily amount to a serious dereliction of duty to the Court. (*Harley*, para 60.)

Section 112(1)(c) of the Law Practitioners Act 1982 sets out the degree of incompetence at which discipline may be imposed. Where the Tribunal:

> (c) Is of the opinion that the practitioner has been guilty of negligence or incompetence in his professional capacity, and that the negligence or incompetence has been of such a degree or so frequent as to reflect on his fitness to practise as a barrister or solicitor or as to tend to bring the profession into disrepute ...

Errors of judgment will never be enough to warrant such an order. In *Y v M* [1994] 3 NZLR 581, 587 a lawyer filed affidavits in family proceedings which contained detailed allegations of sexual abuse by a father of his children without inquiring as to whether they could be substantiated and in breach of certain practice directions. It was there found that although the lawyer had acted inappropriately in breaching the rules of professional conduct and failing to follow practice directions there was no serious dereliction of duty. The Court found that the failure of the lawyer could:

> fairly be described as an error of judgment brought about by too ready an acceptance of what a client says, and by the sense of urgency which seemed (to the partner) to be surrounding the matter (p 590).

In reaching this finding the Court adopted the words of Lord Denning MR in *R & T Thew Ltd v Reeves (No 2)* [1982] 3 All ER 1085 at 1089 where he stated:

> The cases show that it [the jurisdiction] is not available in cases of mistake, error of judgment or mere negligence. It is only available where the conduct of the solicitor is inexcusable and such as to merit reproof.

Causation

Even if it is shown that the lawyer in question is guilty of serious dereliction it must still be shown that the acts have caused additional costs to be incurred. While the award is intended to punish the lawyer for the failures, it is also intended to compensate the litigant who has had to go to extra expense. It must therefore be shown what additional costs have been incurred. This approach has been adopted in New Zealand in *Stephens v Stephens* [1991] 1 NZLR 633, 638 where it was held that the only conduct which could be criticised was failing to inform the other side that the litigant was in receipt of legal aid. Because this failure did not add to costs therefore no order was made.

Discretion

Ultimately the Courts have an overriding discretion in these matters to make or not make such orders.

> Even if the Court is satisfied that a legal representative has acted improperly, unreasonably or negligently and that such conduct has caused the other side to incur an identifiable sum of wasted costs, it is not bound to make an order, but in that situation it will of course have to give sustainable reasons for exercising its discretion against making an order (*RICS v Fryer*).

The Courts rarely decline to make such an order when it is clear that the other elements of the test have been satisfied. It is therefore difficult to predict what factors might weigh in refusing to make such an order. Where the applicant is guilty of some reprehensible conduct, delay, or obstruction this must surely weigh against them. Similarly if the application, though warranted, is clearly motivated by a collateral purpose an order against the lawyer may not be appropriate. The nature of the proceedings may also be relevant. Where the matter is complex or urgent failings may be more excusable and a punitive order less efficacious. This will especially be the case if it can be shown that the lawyers had taken steps to fulfil their duties, even if ultimately unsuccessful. Where wrongdoers recognise their own breach and take steps to remedy the harm caused this would presumably weigh in their favour.

CONCLUSION

Harley applications are not to be made lightly. Such an order causes significant damage to the individual it is aimed at. It may be financially onerous, and can cause considerable harm to reputation. For these kinds of reasons the Courts are reluctant to make such orders.

Lawyers should also be wary of making or threatening such applications lightly. The English Courts have shown themselves to be alive to the possibility of counsel using such applicatisons as a strategem. It would be ironic indeed if the bringing of such an application were itself found to be a serious dereliction of the duty to the Court so as to make applicants for a *Harley* order themselves liable to its sanctions. ❑

SEARCH UPON ARREST

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finds the common law on an everyday topic far from clear

The law as to search upon arrest and whether such a search is reasonable under s 21 New Zealand Bill of Rights Act 1990 involves tension between relatively clear common law rules as to the inadmissibility of evidence obtained illegally and the more case by case approach evident in more recent general search cases such as *R v Grayson and Taylor* [1997] 1 NZLR 399.

The initial trend of the Court of Appeal as to admitting evidence obtained from illegal searches has seemingly been corrected somewhat in cases such as *R v Anderson* (1997) 4 HRNZ 165 and *R v Ratima* (1999) 5 HRNZ 495 as well as the earlier Court of Appeal sentiment expressed in *R v Laugalis* [1993] 10 CRNZ 350 that if the precondition for the power to search does not exist, then the search is illegal and usually unreasonable.

The classic statement on police power to search upon arrest is the Court of Appeal decision in *Barnett & Grant v Campbell* (1902) 21 NZLR 484. At 491, the Court stated:

> We think it may be taken to be settled law that a constable who is legally authorised to arrest an accused person may, at the time of such arrest, and as incidental to it, seize and take possession of articles in the possession or under the control of the accused person, as evidence tending to show the guilt of such person. This is a power at common law, and exists as an incident to the arrest, and this whether the arrest is one which may be made without a warrant, or, as in the present case, one which can only be made under a warrant, and whether the offence is of the nature of a felony or merely a misdemeanour. It is founded on the right to search a person upon his arrest; and the police are entitled to hold and detain property so taken as instruments of proof against the accused, subject to the right of the proper authority to direct such property to be restored to the accused person if it is found that it is in no way connected with the charge made against him.

The authorities referred to in that case refer to personal search and search of the person's immediate vicinity, not rights to search, for example, elsewhere in the property in which the suspect is located.

In *McFarlane v Sharp* [1972] NZLR 838, 844, the Court of Appeal refused to depart from a holding in *Barnett & Grant* that if a search warrant did not authorise the seizure of evidence relating to illegal things found in premises (for example), then such material could not be taken unless there was a contemporaneous arrest of person/s connected with such evidence. Importantly, the right to search and seize is dependant not upon the right to arrest but upon the fact of arrest; see *R v Johnson & Browne* (1994) 2 HRNZ 183, 189-191. This is at least the case if police deliberately omit to seek a warrant directed to a particular suspected offence and articles related to it and then enter premises for the very purpose (even if amongst other purposes) of looking for such articles. This is different from the law in England and Wales: *Chic Fashions Ltd v Jones* [1968] 1 All ER 229 and *Ghani v Jones* [1969] 3 All ER 1700, 1703, which line of authority was followed by Hillyer J in the search without warrant case *R v Taylor* (1993) 9 CRNZ 563.

Tompkins J canvassed the relevant case law on search incidental to arrest in *Craig v A-G* (1986) 2 CRNZ 551, 560 ff. He referred to the judgment of Donaldson LJ in *Lindley v Rutter* [1981] 1 QB 128 where police were held not to have exercised their required discretion when they searched, pursuant to a blanket policy, every person taken to their holding cells. *R v Naylor* [1979] Crim LR 532 was referred to where it was stated that police officers have a very limited right to search a person lawfully in their custody. They may search for and remove objects which they reasonably suspect to be connected with a criminal offence committed by the person. They may search for and remove any object with which a person might do herself or others injury, or they may remove a tool which could be used to effect escape (seemingly a lower threshold is involved than reasonable grounds for belief on the part of police).

Donaldson LJ said at 134:

> It is the duty of any constable who lawfully has a prisoner in his charge to take all reasonable measures to ensure that the prisoner does not escape or assist others to do so, does not injure himself or others, does not destroy or dispose of evidence and does not commit further crime, such as, for example, malicious damage to property. This list is not exhaustive, but it is sufficient for present purposes. What measures are reasonable in the discharge of this duty will depend upon the likelihood that the particular prisoner will do any of these things unless prevented. That in turn will involve the constable in considering the known or apparent disposition and sobriety of the prisoner. What can never be justified is the adoption of any particular measures without regard to all the circumstances of the particular case.

Then *Brazil v Chief Constable of Surrey* [1983] 1 WLR 1155 was considered in which Goff LJ stated the further proposition that a person is not to be searched without being told the reason unless the reason is obvious in the circumstances or the giving of a reason is impossible.

In *Craig v A-G*, Tompkins J said at 562:

> The Police have, at common law, the right to search a person on his arrest. A search involves an infringement of a person's right to freedom and privacy. It can cause embarrassment. It can be regarded as an indignity. So the Police should only exercise the right to search on arrest for good reason. The officer must satisfy himself that the search is reasonably necessary. What may amount to good reason or a reasonable necessity must depend on the particular circumstances. The possibility that the arrested person may have a weapon or some other means

of injuring himself or others, something that may facilitate his escape or something that may be evidence relevant to the commission of an offence, are all obvious reasons justifying a search. There may, depending on the circumstances, be others. And I agree with Goff LJ that it accords with current concepts of the rights of the individual that a person about to be searched is entitled to be told of the reason unless that course is impractical or the need to search is so obvious that to state a reason is unnecessary.

But what must be clearly emphasised is that to search an arrested person for no reason other than his arrest is unwarranted and unlawful. That person has unjustifiably had his freedom curtailed and his privacy invaded. Such a search may amount to an assault. It may aggravate damages. It may warrant exemplary damages by way of punishment.

Section 57A Police Act 1958 dealing with police discretion to search those in custody is the only relevant statutory provision. Subsection 5 indicates nothing limits or affects the right at common law of a constable to search any person upon that person's arrest. Section 315 Crimes Act provides for the manner of arrest, only permitting arrest without warrant in defined circumstances. The power of search consequent upon arrest, is, however, a common law matter.

Mathews v Dwan [1949] NZLR 1037 is authority for the principle that a constable entering upon private premises to execute a warrant of arrest of an individual is justified in insisting on remaining, and endeavouring to see for himself, after being asked to leave, only if the wanted individual be there ie the warrant does not authorise a search to effect an arrest. As was stated by Gresson J at 1042-1043:

> Where, as in this case, [police] have a warrant for the arrest of the person, they may apprehend him, if he is there; but the warrant is no authority to search the premises to see if he is there. In my opinion, a constable entering upon private premises – whether warehouse, barn, dwelling house, or vacant land – to execute a warrant for the arrest of an individual is justified in remaining after being asked to leave only if the wanted individual be in fact there. His authority is to arrest a person; if in fact that person is not there, he cannot, against the will of the owner of the premises remain; he has no authority to search the premises ... I am not prepared to reason from [*Thomas v Sawkins* [1935] 2 KB 249] that a police officer may, against the will of the owner, institute a search of premises merely because he has reasonable cause to suspect that a person subject to arrest is upon those premises.

A recent statement of the reconciliation required between the discretion to search upon arrest and s 21 of the Bill of Rights Act is to be found in *Everitt v A-G* (HC Wellington, 18 April 2000, Gendall J, CP 296/98). The power given under s 57A Police Act to search a person in custody has the purpose of protecting all persons in custody and such institutions and the question was how to achieve the proper balance between this duty to protect and the Bill of Rights duty not to subject persons to unreasonable search. There must be an individual assessment and proper exercise of the searching officer's discretion under s 57A in each case.

The general principle in England and Wales as well as in New Zealand therefore seems to be that the power to search upon arrest is quite confined, although there is tentative obiter from Hillyer J in *R v Taylor* (1993) CRNZ 563, 571 that "it may be" in view of the fact that one of the occupants of premises was arrested and he was a tenant that there could be some justification for the later search of those premises but His Honour did not base his decision on that principle. He relied on the fact referred to above that if police are legitimately on premises and see objects which may indicate that a crime has been committed, police are entitled to take possession of the objects and use them as evidence in relation to a subsequent charge (although, as referred to earlier, seemingly not if there is a search warrant which does not authorise seizure, at least in relation to the particular kind of crime generally as in *R v Briggs* (1994) 12 CRNZ 432, and contemporaneous arrest is not possible). The Police and Criminal Evidence Act 1984 (E & W), ss 17-21, 32, 53-55, 62-63 inter alia allows a search of an arrested person and the premises where he is arrested (or was immediately before he was arrested). Reasonable grounds are required in either case as to danger or escape or for evidence relating to an offence (in the case of a search of the person) or relating to the offence for which he has been arrested (search of premises).

The approach in Canada appears a little more elastic. In *Caslake v The Queen* (1998) 121 CCC (3d) 97, the accused had been arrested in his car after police discovered a bag of marijuana in the grass near a roadway where the accused had been seen. Approximately six hours after the arrest, police went to the garage where the accused's car had been towed, unlocked the car and searched it. They had neither a search warrant nor the accused's permission. Cocaine and cash were found. An officer testified that the search was conducted pursuant to a police policy which required that an inventory be taken of the condition and contents of a vehicle that has been impounded during the course of an investigation. The purpose of the policy was to safeguard the valuables belonging to the owner of the vehicle and to note the general condition of the vehicle. This was, on the evidence, the sole reason that police conducted this search. The car was seen as legitimately the object of the search incident to arrest and it attracted no heightened expectation of privacy. But such a search is only justifiable if the purpose of the search is truly related to the purpose of the arrest (the accused had been arrested near his car). There was stated to be a lesser expectation of privacy in a car than in one's home. It was not seen as necessary independently to establish reasonable and probable grounds to conduct a search incidental to an arrest. A search conducted for the purpose of taking an inventory could be considered a search for a valid objective under the proper circumstances. There was American case law on police power to take an inventory of what they found, to avoid accusations later that they had allowed seized property to become lost or stolen. This type of search was seen as less intrusive than a search conducted for the purpose of gathering evidence (cf the approach evident in *R v Laugalis* (1993) 10 CRNZ 350). Further, the Court of Appeal held in *R v Pointon* (1999) 5 HRNZ 242, 249 that the power to search a vehicle after the arrest of its occupants is a matter of some uncertainty, see also *R v Bainbridge* (1999) 5 HRNZ 317, 325.

Cloutier v Langlois [1990] 1 SCR 158; (1990) 53 CCC (3d) 257 was cited. In that case L'Heureux-Dubé J stated that upon arrest, police have the power to search a person and his or her immediate surroundings for the purposes of guaranteeing the safety of police and the suspect, preventing the suspect's escape, preserving evidence that may be lost or destroyed or merely gathering evidence. (*Caslake*, at 104) L'Heureux-Dubé J referred at 177 to the Ontario Court of Appeal decision *R v Rao* (1984) 12 CCC (3d) 97 where the power to search the person of the arrestee was stated to extend to the premises where he is arrested and which are

under his control so that where a person is arrested in his house, it may be searched for evidence of the crime with which he is charged. At 186, L'Heureux-Dubé J stated:

1. This power [to search incident to arrest] does not impose a duty. The Police have some discretion in conducting the search. Where they are satisfied that the law can be effectively and safely applied without a search, the Police may see fit not to conduct a search. They must be in a position to assess the circumstances of each case so as to determine whether a search meets the underlying objectives.
2. The search must be for a valid objective in pursuit of the ends of criminal justice, such as the discovery of an object that may be a threat to the safety of the Police, the accused or the public, or that may facilitate escape or act as evidence against the accused. The purpose of the search must not be unrelated to the objectives of the proper administration of justice, which would be the case for example if the purpose of the search was to intimidate, ridicule or pressure the accused in order to obtain admissions.
3. The search must not be conducted in an abusive fashion and in particular, the use of physical or psychological constraint should be proportionate to the objectives sought and the other circumstances of the situation.

As stated by Lamer CJC in *Caslake* at 108, the search must be "truly incidental" to the arrest: police must be attempting to achieve some valid purpose connected to the arrest. In *Caslake* (at 116) the degree of intrusiveness was seen as minimal with the search of a motor vehicle seen as less of an affront to the person's liberty, dignity and bodily integrity than even the minimally intrusive body search or frisk search approved in *Cloutier* at 185 or in *Stillman v The Queen* (1997) 113 CCC (3d) 321, discussed below.

In *Cloutier*, the frisk search was validated as it was in order to ensure police safety (see *Stillman* at 371). The statement then as to police power to search to obtain evidence incident upon an arrest was obiter and anyway would not authorise speculative searches merely because a particular suspect, for example, appeared reluctant for police to check his living quarters.

R v Mellenthin (1992) 76 CCC (3d) 481 was an earlier case where there was not an arrest, but a detention. Drugs had been discovered after the accused was stopped at a check stop under a provincial highway traffic act. He was not wearing a seat belt, but otherwise there was no ground for any suspicion of an offence. An officer saw an open gym bag and reflection of what he thought was glass. The accused said that the bag contained food, but a search revealed cannabis resin. The Supreme Court held the discovery inadmissible. Check stop programmes were justified as a means of reducing the road toll but where there had been no prior suspicion that drugs or alcohol were in the vehicle it is not justifiable and reasonable to question the accused about the bag or search it (the arguable point of distinction with *R v Jefferies* [1994] 1 NZLR 290 was that in *Mellenthin*, police had no grounds to suspect drugs or any other serious offence when they stopped the car).

The latest wisdom of the Supreme Court of Canada in a nine Judge, 97-page decision on a hard case is *Stillman v The Queen* (1997) 113 CCC (3d) 321. There was a murder. The accused, aged 17, was arrested. He did not consent to providing bodily samples but police took them anyway under threat of force. The accused used the washroom. He used a tissue to blow his nose and threw the tissue in the waste bin. This tissue containing mucous was seized by police and subsequently used for DNA testing. As there was not enough evidence to charge, he was released five days after, without being charged. Several months later, after receiving the DNA and odontology analysis, police again arrested the accused, in part to obtain better impressions of his teeth. A dentist attended the police station and without the accused's consent took impressions of his teeth. However, the Supreme Court held that although the arrest was lawful, the common law power to search and seize incidental to arrest (which was all that could be relied upon at the time) could not be so broad as to empower police officers to seize bodily samples.

Cory J referred to the power to search incidental to an arrest at pp 340-343 and the Canadian position may from this be stated to be that the power to search upon arrest is not just limited to cases of necessity ie to prevent escape, to ensure safety and to prevent evidence being destroyed.

In fact, the Canadian principle appears to have reached its high-water mark with the Ontario Court of Appeal's decision in *R v Speid* (1991) 8 CRR (2d) 383 where police were entitled to search the car driven by the accused since it was still in the immediate vicinity of the arrest even though the search was not undertaken immediately upon the arrest. There had been a refusal to issue a warrant for the search but police arrested the accused so they could nevertheless proceed with the search.

There is also the decision of the Ontario High Court in *R v Lim (No 2)* (1990) 1 CRR (2d) 136, 145, where Doherty J stated that in his view "in Canada, the justification for a warrantless search as an incident of arrest goes beyond the preservation of evidence from destruction at the hands of the arrested person to include the prompt and effective discovery and preservation of evidence relevant to the guilt or innocence of the arrested person".

Later, however, Doherty JA (as he became) in *R v Belnavis* (1996) 107 CCC (3d) 195 (Ont CA) considered that an arrest for outstanding traffic fines did not then authorise the search of the trunk of a vehicle.

Wherever the limits lay, on the facts Cory J in *Stillman* could not encompass the seizure of bodily samples in the face of a refusal to provide them. Cory J wrote for five Judges and the ultimate finding (6-3) was that the impugned evidence was not admissible, apart from the mucous sample as police, inter alia, could have obtained a search warrant to cover the contents of the rubbish container. L'Heureux-Dubé J was one of the dissenters on the main finding.

In summary, it appears that police power to search incidental to arrest involves a discretion still in New Zealand, England or Canada but that the Canadian Courts have allowed some latitude as far as searches outside the objectives referred to in *R v Naylor* [1979] Crim LR 532 are concerned. The extent of the power to search for articles in the arrested person's possession or control in terms of *Barnett & Grant* is also not free of doubt. The traditional approach was that evidence obtained in breach of the long-held common law principles was inadmissible but this is not necessarily the case now with the Court of Appeal referring to a weighing of factors (albeit with not every illegality being excused on the basis of the ends justifying the means). It may be that this flexible approach will find expression also in the policy approach taken to the extent of what police may do following an arrest. This may also involve consideration of the circumstances and the seriousness of the investigation and the objectives involved. ❑

LITIGATION

COSTS

with
Andrew Beck

DISBURSEMENTS

The touchstones of the new High Court costs rules are predictability and speed: R 47(g). The theory is that, once a proceeding has been assigned to a particular category under R 48, it will be possible for the parties to sort out the costs consequences without having to approach the Court for a further decision. By and large, the rules appear to have achieved their objectives, and the process seems to be operating smoothly. An awkward issue has, however, arisen in connection with the entitlement of a successful party to claim its disbursements.

Two diverse issues have recently confronted the Courts regarding application of the costs rules. One concerns the scope of disbursement claims; the other relates to recovery rates under the Proceeds of Crime Act.

Statutory provisions

Disbursements are provided for in item 11 of the Third Schedule to the rules. This item makes specific allowance for witness fees, agency charges, service charges, binding the common bundle, and ordering, paginating, preparing index for and photocopying the common bundle. The remainder of disbursements fall under the general rubric "other necessary payments". This language is precisely the same as that in item 34(d) of the old Second Schedule. The obvious inference is that the previous approach to disbursements was intended to continue, and that the new items relating to the common bundle are to be seen as additional to the traditional disbursement claim.

It is of some interest that amount which can be claimed for preparing the common bundle is the "cost per page as stipulated". This is an entirely novel way of approaching disbursements, and it is not clear precisely what is entailed; presumably the Court has to fix a per page figure to cover all these aspects of preparing the bundle (see below).

As noted by McGechan J in *Holden v Architectural Finishes Ltd* (1997) 10 PRNZ 675, the expression "disbursements" has become something of a term of art, and the general approach of the Courts has been to allow disbursements in full, rather than awarding only a reasonable contribution to the expenses incurred. He considered that (681):

> An allowance for "disbursements" is intended to cover out of pocket expenses directly related to the particular litigation concerned, as contrasted with indirect expenses or general overheads.

By disbursements, solicitors understand all those items for which a charge is made over and above professional fees. The traditional items included are photocopying, toll calls, courier charges, travel expenses, and witness fees. When it comes to claiming these from an unsuccessful party, witness fees occupy a special position because they are subject to regulation. The remaining items would generally be regarded as standard; the only question is whether they can be described as "necessary" in respect of a particular proceeding.

Auckland's new deal

This approach has now been subject to revision by the Auckland High Court registry. In *Reece v Buchanan* (unreported, HC Auckland M1589/98, 22 June 2000, Chambers J), the standard policy of the Registrar was reported to the Court as not permitting photocopying as a disbursement unless the photocopying was done for the common bundle, or there were exceptional circumstances justifying photocopying being done by an outside agency for which a charge was incurred. The Court apparently accepted this policy, and saw no reason to depart from it in the circumstances before it. It therefore disallowed a claim for photocopying.

The Court also refused a claim for faxes. Chambers J held that these constituted part of office overheads and said (para 16):

> It is, after all, entirely discretionary on the lawyer's part as to whether he wishes to charge the client a separate fee for the cost of sending and receiving a fax or whether he subsumes that indirect expense within general office overheads. He can adopt whichever course best suits him, but his choice should have no effect on what the other party has to pay on a costs award by way of disbursements.

A similar course was followed in *MESB Berhad v Lu* (HC Auckland CL12/98, 27 September 2000, Fisher J). In that case, the argument was raised that tolls, courier charges, travel expenses, photocopying, postage, library research, binding and overtime secretarial services all fell within the category of indirect expenses or overheads. Fisher J allowed only the costs of photocopying the agreed bundle and the case bundle, and said (para 15):

> I do not doubt that the other expenses were incurred but in my view they fall within the category of indirect expenses or overheads which are more generally absorbed in the main scale costs. It may well be that this issue ought to be fully argued and judicially resolved at some time in the future but I am not inclined to delay this costs ruling any further to

call for further submissions on the point.

It is certainly correct that the issue requires to be resolved, and it seems that Fisher J was somewhat uneasy with the blanket approach presented to him. The problem is that the amounts involved are generally small, and there is an understandable tendency not to expend vast resources on costs memoranda (for which no fees are recoverable under the Third Schedule).

A principled approach

The Auckland approach is unsatisfactory. It effectively changes the basis on which disbursements have been traditionally recovered, and makes them part of the daily recovery rate prescribed in the Second Schedule. The daily rates were set by the Rules Committee after extensive consultation with the profession. It was never suggested during those consultations that the rates would represent anything other than professional fees. The understanding was that disbursements would be separately charged as before. Given that the provisions governing disbursements in the Third Schedule are virtually identical to those in the old Second Schedule, this assumption seems reasonable.

In *Holden*, McGechan J noted that the reason for a different approach to disbursements (ie full recovery) is not entirely obvious. He said (at 681-682):

> There may be some economic justification on the basis out of pocket items are, at least relatively, beyond claimant's control as to quantum, and the "contribution" restraint policy has less point. It may also reflect the pragmatic reality that the figures involved, expert witnesses' expenses apart, usually are relatively small.

He clearly recognised that the sort of item under consideration involved some outlay, and was therefore different in nature from a professional fee. The principal distinguishing feature appears to be that the items claimed as disbursements are for things which could be purchased from someone other than a legal professional, and which are provided by the solicitor as a matter of convenience. The charges made are unrelated to the legal services being rendered. The fact that the client pays the solicitor for photocopying rather than a commercial printer should make no difference to recoverability.

The point made by Chambers J that it is purely in the solicitor's discretion whether to make charges for faxes is correct, but it is not determinative. The same can be said of photocopying, postage, telephone and travel charges. The real issue is that, if the solicitor used a commercial operator to send a fax, an out of pocket expense would be involved. The charge would be related to the specific quantity of material transmitted; it would bear no relation to the legal services rendered.

There is obviously scope for manipulation of expenses so as to bring them within the rubric of "disbursements", but the overriding requirement is that the payments must be "necessary". There is therefore a discretion vesting in the Court to decide whether the particular expense was appropriate, whether it was related to the case, and whether the charge was reasonable. For example, in *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* (1990) 3 PRNZ 94, Tipping J examined whether it was reasonable for a party to retain counsel from a different centre, and therefore necessary to pay airfares.

Bearing these principles in mind, the various items of disbursements can be considered.

Photocopying

The Courts have, in the past, accepted without question that photocopying charges constitute a disbursement: see, for example *Equiticorp Industries Group Ltd (in stat mgmt) v The Crown (No 2) (Judgment No 49)* [1996] 3 NZLR 685. The important qualification, as noted by McGechan J in *Holden v Architectural Finishes*, is that the photocopying should relate to the proceeding. It is therefore inappropriate, for example, to include charges for copies of letters retained for the solicitor's file. However, charges for copies of discovered documents made for the other side, copies of pleadings made for the other side and for the Court, and copies of bundles of materials and authorities are all clearly related to the proceeding and are properly recoverable.

The only specific item in the Third Schedule mentioning photocopying relates to the common bundle, but it goes beyond mere copying. The intention appears to be to permit additional charges in this respect. Although the item is limited to the "common" bundle, that does not mean that photocopying of other materials is not a necessary payment. In *MESB Berhad v Lu*, Fisher J allowed the expenses of copying of all bundles prepared for use in Court.

Binding

The Third Schedule specifically provides for binding of the common bundle of documents. It is not clear why this should be limited to the common bundle, and why it should be restricted to "documents" (assuming that, in accordance with common parlance, this term excludes case authorities). It has become commonplace for all bundles prepared for the Court to be bound, and this is as much a necessary payment as photocopying. Recovery of the expense should not depend on whether the other party is prepared to agree to a common bundle. All reasonable binding charges should be seen as legitimate disbursements.

Preparation of bundles

Ordering, paginating, preparing index for, and photocopying the common bundle of documents is recoverable on the basis of "cost per page as stipulated". It might be considered that this is purely a labour charge and that the actual cost of photocopies is an additional "necessary payment". However, if one relies on the analogy of purchasing the services from a commercial printer, the charge would be all-inclusive. It would therefore appear that this is intended to be a combination of labour charges and cost of materials. In order for this to be realistic, it would probably have to be in the region of $1 per page, increasing if more than the usual number of copies are required.

This is a rather cumbersome way of calculating disbursements; it would be simpler to retain the traditional method of a charge per copy together with binding expenses. As discussed above, it is also difficult to see why this should be restricted to the common bundle of documents. All bundles prepared for the Court are proper disbursements related to the proceeding.

Toll calls

There do not appear to be any authorities dealing with toll calls, perhaps unsurprisingly because they would frequently be covered by the de minimis principle referred to by McGechan J in *Holden*, and therefore not subject to dispute. As a matter of principle, however, they are not simply "overhead expenses". They are direct charges incurred by the party in respect of a

proceeding. It is a matter of practical reality that parties, solicitors and Courts are frequently at a distance. Communication between the players has to be accepted as part of the cost of litigation, and toll calls are therefore a necessary payment.

Faxes

To some extent, faxes are in the same category as toll calls, because there is often a toll charge associated with them. The additional factor is the charge imposed for a fax beyond the cost of using the telephone line. This is similar to the charge made for copying documents. While it does amortise the solicitor's overheads to a degree, it is a recognised business (non-professional) service for which the client expects to pay. As in the case of tolls and photocopies, fax charges are part of modern litigation and should be recoverable as a disbursement.

Travel expenses

Litigation at a distance is an inescapable reality. This is partly because of the fact that transactions take place in a national market, but also because Courts – particularly the High Court – tend to be centralised. It has to be accepted that travel is part of the cost of litigation. The trend of legal practice has also been towards operating on a national basis, and clients regularly expect their own lawyer to attend to their business rather than engaging an agent who does not have the same commitment to them or familiarity with the matter.

In *New Zealand Magic Millions Ltd v Wrightson Bloodstock Ltd* (1990) 3 PRNZ 94, Tipping J said (at 96):

> This Court has power to allow when appropriate, a reasonable sum for the travel and accommodation expenses of counsel. ... In my judgment a reasonable sum should be allowed under the heading "other necessary payments" because in the circumstances the expenses involved can reasonably be described as necessary payments.

The circumstances relied on by Tipping J were the detailed background possessed by counsel, and the nature, novelty and complexity of the litigation. Since that time, travel for litigation purposes has become increasingly common. Unless a matter is so routine that travel by counsel would be wasteful, a party should not be denied the benefits of its choice of counsel. Reasonable travel expenses should therefore be regarded as necessary payments.

In this respect, it may be noted that in *MESB Berhad v Lu* Fisher J allowed as a disbursement the airfares and accommodation expenses of one of the parties who was not called as a witness, on the grounds that he was entitled to be present at the hearing (para 16). This is simply an acknowledgment by the Court of the fact that travel is to be seen as an integral part of litigation.

Research material

Outlays in respect of research material are often directly related to the conduct of a proceeding. The commonest expense is a charge for unreported judgments, but it is increasingly likely that charges will be claimed for searching databases and retrieval of electronically stored data.

The difficulty here is that some items may result in a benefit which lasts beyond the litigation, for example, the purchase of a specialist text. There may also be an element of discrimination against those firms who have better resources, and have therefore covered the same expense through their overheads.

On balance, it seems to me that the pragmatic approach is to class all this material as part of what is involved in offering professional services. Having proper resources is one of the aspects of professionalism, and a library – or access to one – is part of professional overheads. While it is true that acquiring a particular resource may be directly related to a proceeding, it also becomes part of the professional's resources as a whole. Trying to divide up the benefits is likely to produce a headache for little benefit.

Overtime secretarial services

Charges for secretarial services have never been regarded as disbursements; they are seen as part of the necessary infrastructure required to offer proper professional services. Overtime charges might nevertheless be regarded as falling into a different category in the sense that they are related directly to a proceeding which demands the added urgency.

As in the case of research material, this is best seen as a concomitant of offering professional services. Inevitably a long trial will involve overtime on the part of both professional and secretarial staff, but that is simply part of the process of providing professional services of this type. It should not be seen as an additional outlay for the party, or as a recoverable disbursement.

Conclusion

There is a real danger that claims for disbursements could be blown out of proportion to their importance, and generate ever lengthier costs memoranda. This would be an extremely unfortunate side-effect of the new costs rules. A settled practice is therefore required with some urgency.

It would not be right to disregard all but a rigid minority of claims for disbursements. That was not the intention of the rules, or the categories set out in the Third Schedule. The ultimate test must be whether any payment incurred by a party was:

- directly related to the litigation;
- necessary for the litigation; and
- in respect of a reasonable charge.

PROCEEDS OF CRIME ACT

The main aim of the Proceeds of Crime Act 1991 is to ensure that "crime doesn't pay" (*Solicitor-General v Nathan* (1999) 17 CRNZ 496, 497). It achieves this by providing for the confiscation of the proceeds of serious criminal offending. The Act allows for property tainted by such an offence to be forfeited to the Crown, and for pecuniary penalty orders to counteract the benefits derived from the commission of an offence. Both remedies are only available after conviction. Pending a conviction, the Crown may apply for a restraining order to prevent dissipation of property. Property which is restrained is held by the Official Assignee pending resolution of the case.

Nature of proceedings under the Act

While the remedies under the Act therefore have their origins in the criminal law, applications under its provisions occupy a curious middle ground procedurally. They are formally civil proceedings, and are brought as originating applications in the civil jurisdiction. They are provided for by R 458D(i)(xvii) of the High Court Rules, and by the Practice Note governing originating applications in the District Courts: [1993] DCR 721.

The Court of Appeal has declared that all proceedings are either civil or criminal (see *Comalco NZ Ltd v Broadcasting Standards Authority* (1995) 9 PRNZ 153). Notwithstanding that, it has conceded that the Proceeds of Crime Act represents an "unusual

hybrid" between the civil and criminal: *Black v R* (1997) 15 CRNZ 278. In that case, the Court considered applications for forfeiture orders to be part of the criminal justice system, even though they are commenced under the High Court Rules. In *Newton v Solicitor-General* unreported, HC New Plymouth M49/99, 23 February 2000, Anderson J held that applications for restraining orders are civil proceedings, governed by the High Court Rules.

It seems clear that, while applications under the Act may occupy an awkward position conceptually, there is no doubt that they are to be commenced as civil proceedings. This is of considerable importance when it comes to the issue of costs.

Applications under the Act generally have one thing in common: counsel for accused persons are eager to have part of any restrained asset designated for payment of their fees. Section 42 of the Act permits the Court to make a restraining order subject to such conditions as the Court thinks fit, including provision for meeting out of the property:

> The person's reasonable expenses in defending any criminal proceedings (including any proceedings under this Act).

This was described as the "legal funds exception" by Chambers J in *Solicitor-General v Nathan* (1999) 17 CRNZ 496. The issue which arises is how a proper rate for such fees is to be determined.

The *Panzer* decision

In *Solicitor-General v Panzer* (unreported, HC Auckland M158-IM00, Cartwright & Tompkins JJ), a Full Court was constituted to decide the most appropriate way of assessing the expenses of counsel where a legal funds exception has been granted. The Court considered various possible methods of assessment:

- current market rates obtained by survey;
- submission of an account to the Official Assignee by the counsel concerned;
- submission of an account to the Law Society or subcommittee appointed under the Legal Services Act 1991;
- submission of an account to the Registrar for taxing under RR 54-59 of the High Court Rules;
- applicable legal aid rates pursuant to the Legal Services Act;
- fixing a rate based on the Crown Solicitors Regulations.

The Court immediately set to one side as undesirable those methods which could only result in a determination of a recovery rate after the event. It also rejected reliance on actual market rates, which could vary significantly and be difficult to determine. Ultimately, it sought to achieve a balance between applicable legal aid rates and the actual fees likely to be charged. Paying less than actual fees was seen as appropriate because the fees would be paid out of what could end up as public moneys, and there would be the added advantage conferred by the certainty of prompt payment. No justification was provided for paying more than the legal aid rate. Presumably this is because the restrained funds technically remain the property of the defendant until forfeited, and should therefore be available to pay for the defendant's counsel of choice.

The method of assessment finally approved by the Court was to take the senior Crown Solicitors rate as a starting point, and apply a percentage factor to recognise that the economies of scale available to Crown Solicitors would not apply to those in private practice. The rates therefore work out as in Table 1:

Status of counsel	per hour	per half day
Senior (150% of rate)	$250	$1000
Intermediate (120% of rate)	$200	$800
Junior (97.5% of rate)	$163	$652

These fees would be subject to a maximum of ten hours for preparation, subject to any order to the contrary being made by the Court at a preliminary hearing stage. An application for second counsel would also be permissible at that time, but the Court was quick to discourage more than one application for departure from the scale.

The High Court Rules

The solution chosen by the Court has to be commended as a pragmatic and robust approach. Given that Anderson J had held in *Newton* that R 46 of the High Court Rules was applicable to applications for restraining orders, it is a little surprising that no consideration was given to the rates set out in the High Court Rules, which were the product of a fairly extensive survey by the Rules Committee. Those rates are based on two-thirds of market rates, so the actual rates would be roughly as in Table 2:

Category under R 48	per hour	per half day
Category 3	$356	$1425
Category 2	$244	$975
Category 1	$160	$638

There are no doubt reasons for not adopting exactly the same rates. While applications for restraining orders may be civil proceedings, the legal funds exception covers expenses in respect of the criminal trial as well, and having two different rates would be unnecessarily complicated. It may well be that market rates for complex civil matters are higher than those for comparable criminal matters. However, if a costs order were to be made against the Solicitor-General in an application for a restraining order, recovery would be based on the R 48 categories, which suggests that they would provide a useful starting point.

The other significant difference in approach is that the categories in the High Court Rules are deliberately focused on the complexity of the proceeding, rather than the seniority of counsel. The theory is that there should be no advantage in employing a silk to apply for an undefended bankruptcy order; it is the nature of the proceeding which justifies a higher or lower scale.

In contrast, the scale for proceeds of crime matters is now linked to the status of counsel. The Court noted that, in cases of doubt, reference could be made to the categorisation of counsel for the purposes of the Legal Services Act 1991 (para 23). This may reflect the idea that there is a general right to counsel of choice, but it goes against the point (stressed by the Court at para 17) that the legal funds exception in s 42 relates only to reasonable expenses. Reasonableness requires that some consideration be given as to the appropriate level of counsel to be instructed in the proceeding.

Conclusion

All things considered, it may have been a better approach to adopt the established categories of the High Court Rules as a starting point for determining the appropriate rates to be allowed for expenses under the Proceeds of Crime Act. This would have had the advantage of consistency of approach and uniformity with existing provisions. ❑

TAX COMPETITION AND NEW ZEALAND

Ross Fazzini, Brookfields, Auckland

considers the implications of the OECD cartel for New Zealand's future tax system

This is the second article in a two-article series discussing tax competition issues. In the first article entitled *Harmful Tax Competition?* [2000] NZLJ 412 we saw that tax competition between countries has motivated the OECD to try to curb what it calls "harmful tax competition". In that article it was concluded that the OECD's response to harmful tax competition is anti-competitive and contrary to the OECD's own economic philosophy. This article considers the future of tax systems in light of globalisation and the increase in tax competition that comes with it. It also suggests some solutions to the problem of designing a more appropriate tax system for New Zealand.

EFFECTIVENESS OF OECD'S RESPONSE

We saw in the first article in this series that the OECD's response to globalisation and international tax competition has been an attempt to quash tax regimes that the OECD considers employ harmful tax competition policies. Two OECD member countries, namely Luxembourg and Switzerland, abstained from adopting the report entitled *Harmful Tax Competition: An Emerging Global Issue* ("the report"), calling it "partial and unbalanced" (Luxembourg at p 74 and Switzerland at p 76 of the report). The following comment from the statement made by Switzerland appears at p 78:

> ... the selective and repressive approach that has been adopted does not give territories that make tax a pillar of their economies an incentive to associate themselves with the regulation of the conditions of competition and will therefore fail to combat effectively the harmful excesses of tax competition that develops outside of all rules. On the contrary, it could reinforce the attraction of offshore centres, with all the consequences that this implies.

The author concurs with the sentiment that the OECD's response to harmful tax competition may be ineffective. It is contended that the reason for this is that the OECD is misguided in focusing on erosion of the tax base of its member countries. In the author's view the problem is not that any particular country's tax base will be eroded (though that will happen), rather the problem is the inability of our present tax systems to cope with a global liberalised economy and the necessary consequences that flow from it. This misapprehension of the problem will ultimately mean that the actions of the OECD are ineffective. The OECD may be successful in slowing the erosion of its tax base, however it will also be successful in slowing the progress to a new tax system that meets the needs of a global economy.

GLOBALISATION AND THE UTOPIAN TAX WORLD

Business is global and is no longer confined within the jurisdictional boundaries we call countries. Taxation, however, in its present form is uniquely territorial. A country will generally have the right to tax only those sources that have a sufficient nexus with the country. In relation to income, for example, a country will generally only have the right to tax income produced in the country or produced by a person resident in the country. An attempt to tax income outside these bounds might be seen as international theft.

A Utopian tax world might involve sustained multi-lateral agreement between all countries whereby each country contributes its entire tax revenue to a central organisation which would then reallocate the worldwide tax revenue among the world's countries. This would be done in a manner that compensated each country for the cost of providing standard public benefits to its citizens. Thus a standardised worldwide tax could be imposed. This would eliminate the primary incentive for countries to lower their tax rates since they would no longer need to attract tax sources to secure tax revenue.

The problem with this, as with all grand bureaucracies, is that it just would not work. Amongst the primary reasons for this is that within a country (and even within regions or populations within a country) people demand sovereignty. A corollary of sovereignty is the right to choose how to raise taxes, what quantum of taxes to raise and how to spend those taxes. With a standardised worldwide tax this sovereignty would be lost. In addition, it is contended that there would be incentive for countries to cheat and under-tax their own citizens, since this would mean that they pay less tax and might still be able to receive the amount of tax revenue that they require from the central organisation. It is these types of problems that will prevent any standardised worldwide tax becoming a reality.

The OECD opines at p 20 of the report that "globalisation has had a positive effect on the development of tax systems, being, for instance, the driving force behind tax reforms which have focused on base broadening and rate reductions, thereby minimising tax induced distortions". It is arguable that the contrary is true. Globalisation has had a negative effect on the development of tax systems by making it easier for people to use tax havens and pay less tax. The base broadening has not worked because those sources that are mobile can easily be transferred to tax havens. The question is whether, as a response, there should be a base narrowing or a base shifting so that only those activities that place a cost on a country are subject to tax.

TAX REVIEW

On 5 October 2000 Finance Minister Michael Cullen announced the terms of reference of a public inquiry into the New Zealand tax system ("the review"). The purpose of the review is to provide the government with an appropriate framework within which to build tax policy. The main functions of the review will be:

(i) to examine and inquire into the structure and effects of the present tax system in New Zealand; and

(ii) to formulate proposals for improving that system, either by way of making changes to the present system, abolishing any existing form of tax, or introducing new forms of tax.

The review will concentrate on how to ensure a sustainable and continuous flow of revenue to meet government requirements in the face of changing economic, social and technological conditions. It will form the basis of advice to the government about whether the tax system can be improved.

One task will be to assess the extent to which the tax system can contribute to broader social and economic objectives such as encouraging secure, high quality employment, generating a fair distribution of income, maintaining a sustainable environment and promoting higher savings. It will do this by recommending structural changes for the tax system, if these are appropriate. The review is to consider the best mix between different tax sources such as income, consumption, financial transactions and wealth. A question faced by the review, and considered in this article, is whether the tax system and tax rates need to be modified in light of new technology and international competition. The review will submit its final report to the Minister by the end of September 2001.

NEW ZEALAND'S FUTURE TAX SYSTEM

It was mentioned in the terms of reference of the review that ideally a tax system should raise revenue simply, efficiently, fairly and reliably in an environment of changing technology, growing globalisation and increasing complexity and in ways that do not materially undermine the environment, social cohesion or the effective use of resources.

Historically the rationale of tax systems was that a country had the right to tax any income that was derived from that country, regardless of whether or not the country bore any cost in generating that income. With the advent of globalisation and the internet revolution we are seeing the "melting of the glue" (this phrase is borrowed from *Blown to Bits* by Peter Evans, which provides an excellent account of how globalisation and the internet are changing the nature of both business and our daily lives) that binds together the geographical location of a person and the place where that person generates or derives income. It is contended that for a tax system to raise revenue simply, efficiently, fairly and reliably in the future it will need to adopt an approach that equates the right to tax a particular tax source with the cost a country incurs in relation to that tax source.

For New Zealand's future tax system tax rates should be market specific, so that they relate to the tax source upon which they are imposed. Tax rates, like the price in any market, should be free to move in an internationally competitive fashion and should be set by each state at a level that allows the state to cover its costs of admitting that tax source. This should result in an efficient tax system and should solve the problem of tax base erosion caused by the relocation of mobile traditional tax sources to tax havens. It might mean the introduction of new taxes in relation to residents or increases of existing personal income tax rates, since these are sources that impose costs on a country.

At the Canadian Tax Foundation's first World Tax Conference held in February and March 2000, Graeme S Cooper of the University of Melbourne conducted a "lottery" which invited conference attendees to "pick the date on which the last OECD member country will abolish the corporate income tax". Cooper indicated that an earlier conference speaker, Roy Chowdhury, had already entered a bet on ten years and that fellow panellist Jack M Mintz of the Howe Institute, Canada, had suggested twenty [2000] *Tax Notes International* 1063. Mintz is quoted as saying:

> The corporate income tax is in deep trouble and I think there are genuine questions as to whether it can survive 20 years.

These predictions conform with the thesis that taxes should reflect the marginal cost to a state of admitting particular tax sources. Companies themselves do not impose significant costs on a state. Rather it is their activities and employees which impose costs. From an efficiency perspective there should be no problem with abolishing corporate income tax in New Zealand provided it is replaced with something more appropriate. One solution might be to abolish income tax at the corporate level and simply continue to tax shareholders on any dividends received from the company. Immediately the problem of tax deferral is raised, however attribution rules similar to our Controlled Foreign Company rules and Foreign Investment Fund rules that attribute income of particular companies to shareholders might equally apply to all New Zealand companies. A positive result that might flow from such a policy is increased incentives for foreign investment in New Zealand. This might in turn result in an improved labour market and encourage the return of New Zealand's skilled talent.

If New Zealand can move quickly to a new tax system we might also benefit from a first mover advantage by competing for foreign tax sources at a time when other countries are shackled with tax systems of a bygone era.

NEW ZEALAND'S OECD OBLIGATIONS

In moving to a new tax system New Zealand will need to be mindful of its OECD obligations, particularly in light of New Zealand adopting the report. The tax policies propounded in this article should not offend the OECD, since the OECD agrees that some tax competition is acceptable. Acceptable tax competition occurs where countries with specific structural disadvantages, such as poor geographical location and lack of natural resources, use special tax incentives to offset non-tax disadvantages (see p 15). The policies outlined here are designed to offset New Zealand's specific structural disadvantages, including New Zealand's geographical location (a disadvantage for some purposes), New Zealand's small national economy, exchange rate vulnerability, and depleting labour talent.

CONCLUSIONS

There is little doubt in the author's mind that we are on the brink of introducing new tax systems into New Zealand and around the world. New tax systems will account for the global economy and international competitiveness for tax sources. To this end the author implores the review to begin carte blanche when redesigning New Zealand's tax system, so that the result is a cohesive and efficient system that will meet New Zealand's needs well into the 21st Century. ❑

EXAMPLES IN LEGISLATION

Hannah McKechnie, the University of Otago

looks at the PPSA as an example of the use of examples

The Personal Property Securities Act 1999 (PPSA) contains worked examples. The examples are set out in a separate paragraph after almost every substantive provision. Section 78 is a typical provision.

> *Priority of Security Interests in Accessions*
>
> **78. Security interests in accessions**—A security interest in goods that become an accession continues in the accession.
>
> **Example**
> A security interest in a motor continues in the motor even after its installation in a car.

The use of examples in this way is a novel concept in New Zealand legislative drafting. Although examples have sometimes been embedded in the text of statutes in the past, the PPSA is the first Act to use them with such frequency and set them apart from the text of the section.

The purpose of a statute is to communicate the law. It is essential that this is done effectively, especially since the ignorantia juris neminen exusat principle applies in New Zealand. Ignorance of the law is no excuse. However, the assumption that the public knows the applicable law is only fair if the law is communicated in a way that people can understand. Legislative examples are a tool that the drafter can use to facilitate comprehension of legislation.

This paper will begin by looking at how legislative examples have been used in other jurisdictions, before exploring the background to the examples in the PPSA. It will then consider the status of the examples in the Act and their role in statutory interpretation. The final section will investigate whether examples should be used in the PPSA and analyse whether they will help or hinder the understanding of the statute.

OVERSEAS JURISDICTIONS

Examples in legislation were pioneered in India (Elliott, "Using Examples in Legislation", (1993) 28 *Clarity* 18). They were a key feature of the codes drafted in the late nineteenth century. The English drafters were free from the traditional constraints on the format of British legislation. They were also aware that many people using the codes would have little formal legal training. As a result, examples were often included to help the readers understand new legal concepts (Elliott, 1993).

The Indian Evidence Act 1872, drafted by Sir James Fitzjames Stephen, is a notable example of such a code. It repealed all previous rules of evidence and introduced new rules based on principles of English law. Almost every substantive section of the Act is followed by a number of illustrations. As in the PPSA the illustrations are contained in distinct paragraphs rather than embedded in the text.

In almost every instance Stephen formulated the examples from cases actually decided by the Courts in England. He reasoned that the examples "not only bring into clear light the meaning of abstract generalities, but are, in many cases themselves the authorities from which rules and principles must be deduced" (Stephen, "*Digest of the Law of Evidence*" 4th ed (1893) at viii). The examples were often used to interpret the rules of evidence but, interestingly, they were not regarded as part of the sections themselves (*Mohomed Syedol Ariffin v Yeoh Ooi Gark* [1916] 2 AC 575 at 581).

In 1873 Stephen drafted a similar Evidence Act for England. It also contained a number of examples but, despite the support of the Attorney-General, was never tabled in Parliament.

In more recent times the UK Parliament has approved the incorporation of examples into several pieces of legislation, such as the Occupiers Liability Act 1957, Consumer Credit Act 1974, Race Relations Act 1976 and the Torts (Interference with Goods) Act 1977. In most cases the examples are embedded in the text of the sections.

The Consumer Credit Act 1974 makes extensive use of examples. A series of examples are set out in the second schedule, rather than the body of the Act, followed by analysis of each example. At the beginning of the schedule there is a table that relates the examples to the sections that they are illustrating. Section 188 sets out the status of the examples. They are neither exhaustive nor are they to prevail if they conflict with any provision of the Act. The wording in this section is similar to the section that sets out the status of the examples in the PPSA.

The Canadian legislature has included examples in several statutes. Section 6 of the British Columbia Surveys Act even gives an example in the form of a diagram. This is a technique recommended by the New Zealand Law Commission (*The Format of Legislation*, NLCR 27, 1993, 54) and specifically mentioned in the Interpretation Act 1999.

The Indian Evidence Act, 1872. 209

153. When a witness has been asked and has answered any question which is relevant to the inquiry only in so far as it tends to shake his credit by injuring his character, no evidence shall be given to contradict him; but if he answers falsely, he may afterwards be charged with giving false evidence.

Exclusion of evidence to contradict answers to questions testing veracity.

Illustration.

(*a.*) A claim against an underwriter is resisted on the ground of fraud.

The claimant is asked whether, in a former transaction, he had not made a fraudulent claim. He denies it.

Evidence is offered to show that he did make such a claim.

The evidence is inadmissible.

(*b.*) A witness is asked whether he was not dismissed from a situation for dishonesty. He denies it.

Evidence is offered to show that he was dismissed for dishonesty.

The evidence is not admissible.

Examples in statutes have also recently become a feature of Australian legislation. The Australian Interpretation Act 1901 even makes express provision for their status in s 15AD. The formulation of this section is similar to s 21 of the PPSA. It provides that the examples are not exhaustive and that the section prevails in the case of inconsistency with the example. Examples were also specifically recognised as a legitimate drafting tool by former Australian First Parliamentary Counsel, Ian Turnbull, in one of his drafting instructions (No 7 of 1988).

The examples in the PPSA were actually inspired by the type of examples used in the Queensland Domestic Violence (Family Protection) Act 1989. The illustrations in this Act are separated from the text of the section similar to the codes of India. However, in contrast to the PPSA most sections are followed by more than one example, which appear to be based on actual cases.

Legislative examples have had a resurgence in recent years, especially in Australia. They have been accepted as a valuable drafting tool in several jurisdictions. New Zealand has followed overseas drafting precedent.

NEW ZEALAND LEGISLATION

Prior to the PPSA New Zealand had a number of statutes that contained examples. Recent examples include the Accident Insurance Act 1998 (ss 32, 60, 283) and the Year 2000 Disclosure Act 1999 (s 6). However, all of the examples in legislation prior to the PPSA were embedded in the text of the sections. They were not set out as a separate part of the Act and no guidance was given as to their interpretation.

The PPSA was drafted at a time when the morphology of the statute book was changing rapidly and greater emphasis was being placed on public access to the law. There have been a number of recent reviews of legislative drafting, printing and typography techniques. In 1993 the Law Commission published a report on the format of legislation. It considered how the format and design of statutes could improve public access to the law (NLCR 27, 1993). In that report the Commission expressly supported the use of examples as an aid to understanding. The Commission also released a Legislation Manual in 1996 (NLCR 35, 1996). It promoted plain language drafting to aid public understanding and make the law more accessible. The Parliamentary Counsel Office has also conducted several surveys relating to the clarity and accessibility of legislation. This has led to a change of the typeface of statutes effective from 1 January 2000.

Both the Parliamentary Counsel Office and the Law Commission have statutory duties to make legislation accessible to the public (s 5(1)(d) Law Commission Act 1985 and s 5 Statutes Drafting and Compilation Act 1920). Yet access to the law is pointless if people can't understand it when they get it. In *VUWSA v Government Printer* [1973] 2 NZLR 21 Wild CJ held that the state is under a legal duty to make statue law physically available to the public. If this is the case, Lawn argues that the state must also be under a duty to make the legislation understandable (Lawn, "Format of Legislation and Access to Law" (1999) NZLJ 418 at 420).

New Zealand drafters first experimented with explicit examples in the explanatory note to the Banking and Insolvency (Netting and Payments Finality) Bill 1998 but they were never used in the Act itself. It wasn't until the more public and frequently used PPSA was drafted that examples were included. This was hardly surprising given the attitude of the Parliamentary Counsel Office and the Law Commission towards clear, accessible legislation.

THE PPSA

Status of the examples

Section 21 of the PPSA sets out the status of the examples in the Act. Every example is part of the Act (s 21(3)) but is only illustrative and does not limit the provision to which it relates (s 21(2)). If a provision and the related example are inconsistent, the provision prevails (s 21(3)). The Interpretation Act 1999 also specifically refers to the use of examples in statutory interpretation. Section 5(2) provides that indications provided in the enactment may be used to ascertain the meaning of the enactment. Examples are expressly included in the list of possible indications listed in s 5(3). Notably, s 5 of the Interpretation Act 1999 permits the use of examples to aid interpretation but does not make them mandatory considerations.

The examples in the PPSA seem to have a peculiar castrated status. Although they are part of the Act their use as an interpretative tool is limited. Furthermore, the Court has discretion whether or not to have regard to them at all.

Some submissions to the Personal Property Securities Bill suggested that s 21(2) and (3) attempt to prevent the examples from affecting the interpretation of the Act at all and that the Court will have the futile task of considering what their function is (Gedye, Submission #15 to the Personal Properties Securities Bill 1999, p 6). This is unlikely to be the case. The principles in s 21 are very similar to s 14AD of the Australian Interpretation Act 1901 and the common

law in India and England. In these jurisdictions examples have proved a valuable tool in the construction of statutes despite limitations on their use.

In Indian common law examples do not exhaust the full content of the related section and they can not be used to curtail or expand the meaning of the legislation (*Shambu Nath Mehra v The State of Ajimer* 9 1956) SCR 199). They will be rejected if they are repugnant to the sections themselves, although it was conceded in *Syedol Ariffin v Yeoh Gark* [1916] 2 AC 575 that this would require a very special case. The function of examples is to show how the principle in the section should be applied to a particular fact situation. It was also held to be the duty of the Court to accept examples as being relevant and valuable to the construction of the text if possible.

One difference between the Indian common law and the PPSA is that in Indian law the examples were not considered to be part of the Act. This could potentially give the examples in the PPSA more force than the Indian examples. However, this seems unlikely because the status of the examples is clearly limited in s 21 of the Act. If the Courts are faced with determining the function of the examples in the PPSA Indian common law will be a useful guide.

The prevalence of the provision over an inconsistent example in s 21(3) of the PPSA may create some uncertainty. Until a provision is interpreted it will not be known whether or not the example is inconsistent. Yet, an example can be used to help interpret the relevant provision (s 5(2) Interpretation Act 1999). This is a circular argument. Although repugnant examples will be rare, there could potentially be situations where the Court will not be able to reconcile these two provisions.

This problem could have been avoided if the examples in the PPSA were given equal status with the other parts of the Act. After all, the examples have been through the same process. They have been scrutinised by drafters, select committees, those making submissions and finally Parliament. Therefore, they should be able to influence interpretation to the same extent as the rest of the Act. The drafters seem to be clinging to the traditional preference for statements of general principle over concrete examples. They have had the courage to include examples but have been too cautious to give them much weight. This is a mistake. Giving the examples full status would not lead to chaos. The meaning of each section would still have to be ascertained from its text in light of its purpose, due to s 5 of the Interpretation Act 1999. Giving examples only a subsidiary status is sure to cause nothing but confusion.

Analysis of the examples

Examples were included in the PPSA to make the statute easier for the public and professionals to understand and apply. It is especially important that people have access to the PPSA because it is a major overhaul of the law in this area. The PPSA abolishes existing regimes contained in the Chattels Transfer Act 1924, Motor Vehicles Securities Act 1989 and the Companies Registration of Charges Act 1993 and almost completely codifies the law in this area. It is a piece of legislation that will affect a large percentage of the public so it is important that it can be readily understood by all. Although the PPSA will be a high use piece of legislation it still refers to a number of complex, abstract legal terms. These terms often have meanings that do not accord with their ordinary meanings. For example, the terms "perfection" and "attachment" are used to describe when a security interest vests in a piece of property. Such terms could be confusing to the reader if not clearly explained. The question is whether the examples in the PPSA add to its clarity and help readers apply and interpret it, or whether they simply mislead and add to the confusion.

Using examples in legislation seems to fit the way that people naturally process what they are reading. Texts can not be understood in isolation. Whenever somebody reads something they apply all of their accumulated knowledge to the text (see Simmonds, "Between Positivism and Idealism", (1991) 50 *Cambridge Law Journal* at 308).

The more background knowledge the reader has, the easier it is for them to put what they are reading into a context that they understand. This is especially true of statutes. Legislative provisions are like abstract formulae that are applied to factual situations. When someone reads a statute for the first time it is natural for him or her to apply it to familiar fact situations. If the reader has legal training or other background knowledge they are more likely to be able to think of appropriate scenarios and understand what the statute means. This process is also used by drafters, who constantly test their work by applying provisions to a series of examples.

Providing examples for the reader in the statute gives the legislation real life effect and makes it seem more tangible. If examples were not given in the text most readers would apply their own anyway. Good examples given in the statute will prevent readers from applying their own false examples. It also makes the ideas behind the legislation more explicit. If the ideas are implicit the legislation may be biased against readers with little background knowledge.

Reaction to legislative examples has been mixed. When Stephen drafted an Evidence Act for England that contained examples it was supported by Lord Coleridge, the Attorney-General. However, it was never tabled in the House of Representatives because there were fears that Parliament would not approve (Elliott, 1996).

A number of Judges have welcomed the assistance of statutory examples. In *Mahomed Syedol Ariffin v Yeoh Ooi Gark* Lord Shaw found them both "relevant" and "useful" in the construction of the text. More recently, Lord Shaw thought examples were "*useful pointers to aid the construction*" of the statute (*Amin v Entry Clearance Officer* Bombay, [1983] 2 AC 818 at 834). Perhaps unsurprisingly, Lord Denning was also a proponent of legislative examples. In *Escoigne Properties v IRC* [1958] AC 549 at 565 he said "one of the best ways, I find, of understanding a statute is to take some specific instances, which, by common consent, are intended to be covered by it".

The majority of the submissions to the Personal Property Securities Bill supported the examples in the statute. Submissions opposing the examples typically came from people with legal training, such as lawyers and academics. They felt that examples did not belong in the text of the statute and will be misleading. A cynic could compare them to the Brahmin in India, who were able control the law by maintaining a monopoly on legal knowledge.

It is possible that the examples in the PPSA could mislead readers. The examples often involve the most simple fact situations. The simplicity of the examples may tempt the reader to rely on them and overlook the text of the section. Statute users may rely on analogy from the example rather than the principle set out in the related provision. As the example can only be of limited assistance in interpreting the provision, and may even be inconsistent with it, the reader

may be completely misled about the effect of the section. Although there is potential for the same situation to arise when examples are embedded in the text of the section, the problem is exacerbated by setting out the examples in a distinct paragraph.

The choice of appropriate examples is crucial if the legislation is not to be misleading. Examples should be very general and should be chosen to complement the provision, not substitute it. The section should be able to stand alone. Overuse of statutory examples can lead to sloppy drafting. Drafters can become over-reliant on the examples to convey the meaning and lack precision in the text of the substantive provisions. This was part of the reason that the Law Commission of India recommended the omission of examples (Rajagopaul, G R, "*The Drafting of Laws*", (1972, Bombay) at 130). Substandard drafting does not seem to be a problem in New Zealand at present but the Parliamentary Counsel Office will have to make sure that examples are only used where necessary in appropriate Acts and do not become a crutch for incompetent drafters.

It is also suggested (Gedye, 1999) that the examples are better included in official commentaries and textbooks, rather then the Act itself. New Zealand's PPSA was modelled on art 9 of the American Uniform Commercial Code. There is a lengthy official commentary to the code that contains a number of detailed examples. There are several advantages in including examples in the commentary to the Act.

Firstly, more examples can be fitted into the commentary than the statute. There is not so much pressure to be succinct so examples can cover a broader range of fact situations. There is also room in the commentary for explanation and analysis of the examples to further aid understanding. Analysis of examples was done with some success in the second schedule to the Consumer Credit Act 1974 (UK). In the PPSA there is only one example given for each provision. It is often the simplest case. The examples do not deal with hard cases so they are of limited use. This can be compared with Australian and Indian legislation that uses several examples for each provision. Perhaps including more examples in the PPSA would make the meanings of the sections clearer.

Secondly, it is easy to change examples in a commentary if they prove to be wrong or misleading, while statutory amendment is necessary to change examples in legislation. As mentioned above, it will not be known whether the examples in the PPSA are inconsistent until the section is interpreted so there is no way of checking whether the examples need to be changed. Even before the PPSA was enacted there was at least one example identified to be wrong at law. Clause 45 of the Personal Property Securities Bill related to the attachment of a security interest in after-acquired property. It gave the example of a car. A car is likely to be classed as a consumer good so no security interest would attach to it at the time of acquisition by virtue of cl 45(2)(a). This error was identified by submissions to the Bill and the example was changed to "equipment". This illustrates that there is a possibility that there are still incorrect examples in the PPSA that will have to be changed in the future. The examples could be changed more easily if they were contained in an official commentary to the Act

New Zealand does not have an official commentary to legislation but it is suggested that textbooks could fill this role (Gedye, 1999). Authoritative textbooks such as Professor Ron Cumming's "*A Handbook on the Saskatchewan Personal Property Securities Act*" (Cumming and Wood, Saskatoon, 1987) have been particularly useful in assisting Canadian Courts to interpret legislation.

However, including the examples in academic textbooks may defeat the purpose of having the examples at all. Examples are used to make the law more accessible to the public by providing them with practical applications of the statute. It is unlikely that many lay-people would have access to legal textbooks. Including examples in textbooks is therefore only helpful for legal professionals who are better placed to understand the legislation in the first place.

Ease of amendment is also a weak argument for including examples in textbooks rather than statutes. If necessary, amendments to the examples in the PPSA could be hurried through Parliament. Acts are often amended after enactment when they are interpreted contrary to Parliament's intention.

The examples in the PPSA are very similar to those used in the Canadian textbooks. For example, the example of commingled goods in the *Alberta PPSA Handbook* (Cumming and Wood, 4 ed, Calgary, 1998) is combining sugar and chocolate to make candy. The example in the New Zealand PPSA is combining sugar and other ingredients to make icecream. In a number of other examples the Canadian text uses a boat while that PPSA applies the same example to a car. The similarity of the examples is not surprising considering that Professor Cumming had some influence over the New Zealand Act. The similarities may be seen to give the Canadian texts some authority to influence the interpretation of the New Zealand statute.

The use of examples in legislation also closes the gap between case law and statute. The examples provide a precedent from a hypothetical case. The difference is that Parliament rather than the Court decides the hypothetical case before the Act comes into force. Unfortunately, due to the limited status of the examples, the precedents in the stature do not carry a great deal of weight. They can not be relied on in argument in the same way as a case because it will not be known whether or not the example is inconsistent with the section.

CONCLUSION

The PPSA is the first New Zealand statute to contain examples that are set apart from the text. This initiative came about as a result of the drive by the Law Commission and the Parliamentary Counsel Office to make the law more accessible. Although the use of examples in this way has been trialed in other jurisdictions it remains to be seen whether the examples in the PPSA will assist the New Zealand public and Courts in interpreting the statute.

Drafting a statute is an exercise in communication English. Any technique that significantly improves comprehension is to be welcomed and embraced. Clear examples in legislation have been approved by the English judiciary and can be especially helpful to people without legal training. Unfortunately, the examples in the PPSA are given a lesser status than the rest of the Act. This is likely to cause uncertainty and confusion. It is also suggested that the Act would be clearer if more than one example was given after each provision. The drafters of the PPSA should be applauded for attempting to make the law clearer and more accessible. However, had they given the examples equal status with the rest of the Act they may have been more successful. ❑

INTERPRETATION ACT 1999

Ernie Pitchfork, Manukau Institute of Technology

thinks there is the possibility of a punch-up between Parliament and Courts

The Interpretation Act 1999 came into force on 1 November 1999 and repealed and replaced the Acts Interpretation Act 1924.

It cannot be said that the Interpretation Act 1999 was introduced with insufficient time for thought, reflection and discussion, as the Act mostly followed the recommendations made by the Law Commission in 1990. Several major alterations to the draft Bill as proposed by the Law Commission were made by the Justice and Law Reform Committee during the Select Committee stage of the Bill. The Bill was referred to the Justice and Law Reform Committee on 2 September 1997, the Committee reported on 4 December 1998 and Royal Assent was given on 3 August 1999. The Act, as befits a piece of legislation of fundamental importance to both the judicial and constitutional system was considered in depth by all those who took part in its formation and evolution: its effects merit similar consideration.

The purpose of the Interpretation Act 1999 is stated in s 2, namely:

> **2. Purposes of this Act** – The purposes of this Act are:
>
> (a) to state principles and rules for the interpretation of legislation; and
>
> (b) to shorten legislation; and
>
> (c) to prompt consistency in the language and form of legislation.

These are admirable aims, so one needs to examine how the 1999 Act attempts to achieve this purpose, and in particular how it differs from the Acts Interpretation Act 1924.

The fundamental section of the 1999 Act is s 5:

> **5. Ascertaining meaning of legislation** – (1) The meaning of an enactment must be ascertained from its text and in the light of its purpose.

This is a change from the corresponding provision of the 1924 Act, s 5(j), which read:

> every Act, and every provision or enactment thereof, shall be deemed to be remedial, whether its immediate purport is to direct the doing of anything Parliament deems to be for the public good, or to prevent or punish the doing of anything it deems contrary to the public good, and shall accordingly receive such fair, large, and liberal construction and interpretation as will best ensure the attainment of the object of the Act and of such provision of enactment according to its true intent, meaning, and spirit.

According to the report of the Justice and Law Reform Committee on the Interpretation Bill (now the 1999 Act), s 5(1) of the 1999 Act merely expresses s 5(j) of the 1924 Act in modern language.

This is, with respect, a statement which is difficult to accept, and indeed which clashes with much of the tenor of the report of the Justice and Law Reform Committee.

One may first note that the words "fair, large, and liberal" do not appear in s 5(1) of the 1999 Act. The phrase was omitted because both the Law Commission and the Justice and Law Reform Committee (and therefore Parliament which accepted the recommendations of the Committee) believe that a purposive approach does not always require a "fair, large, and liberal" interpretation, and that sometimes the purposive approach requires a narrower interpretation. However, and most importantly, the Committee went on to state "The main rationale behind cl [now section] 5(1) is to ensure that the Courts, in accordance with their constitutional role, give effect to the law as expressed by Parliament". It is submitted that this sentence, together with several other aspects of the Justice and Law Reform Committee report, indicate a desire on the part of Parliament to exercise tighter control over the Courts interpretative function where Parliament believes that the Courts are indulging in judicial law making.

One may next note that the two fundamental principles of modern statutory interpretation are "purpose" and "context" (see eg *Hawkins v District Prisons Board* [1995] 2 NZLR 14 in which Hammond J stresses the vital nature of context). The purpose of the 1999 Act is described in s 2 of that Act, and both the Law Commission and the Law Society recommended that the word "context" be included in the 1999 Act to bring s 5(1) of that Act into line with the current approach of the Courts. This recommendation was rejected by the Justice and Law Reform Committee (and by Parliament when it enacted the Bill as amended by the Committee) on the grounds that the word "context" was imprecise and because its inclusion might widen the Courts current approach to statutory interpretation. The Committee stated (and presumably Parliament accepted) that "A direction to take 'context' into account may lead to a more liberal approach to statutory interpretation that departs from the words of the statute and therefore the purpose of Parliament".

There seems here to be clear rumblings of a constitutional clash between Parliament and the Courts, with Parliament afraid that the Courts are usurping their law making powers. Courts in New Zealand have generally taken a wide

approach to statutory interpretation in the past, and have often used the context principle to justify this.

The Courts have used the internal context of the statute to justify a wide meaning. Thus in *King-Ansell v Police* [1979] 2 NZLR 531 the Court held that the word "ethnic" was to have a broad meaning as it appeared in the phrase "colour, race or ethnic or national origins".

Presumably as such an approach does not "depart from the words of the statute" Parliament has no objection to the use of the internal context of a statute.

However, the area in which the New Zealand Courts have shown most creative interpretation in recent years is in the use of materials from outside the statute, ie in the use of what we might call the external context.

The external context includes such matters as other Acts of Parliament, both current and repealed, and any common law that has been superseded by the statute. Again, as in using other Acts of Parliament the Courts will not "depart from the words of the statute", this approach would be expected to find favour in the eyes of legislators.

Perhaps the area to which Parliament is manifesting some hostility is in the use of material which attempts to describe the social and economic situation prevailing when the statute was enacted. Such matters may identify the mischief the Act was intended to remedy and may help to ascertain the purpose of the Act: certainly the use of such material is hallowed by time eg *River Weir Commissioners v Adamson* (1877) 2 App Cas 743. The proving to the Court of the social and economic situation existing at the time may involve a great range of materials. The presentation of such material to the Court has been enthusiastically welcomed by Sir Ivor Richardson, President of the Court of Appeal, who has stated extrajudicially "many counsel seem somewhat reluctant to explore wider social and economic concerns; to delve into social and legal history" (1985) 15 VUWLR 46.

However, in addition to the social and economic environment prevailing when the statute was enacted, the Courts have also taken into account the social and economic environment in which the statute continues to function. In these circumstances it is not surprising that Sir Ivor Richardson's welcoming the presentation of social and economic data to the Court applies to the current environment in which the Court must operate as well as the environment prevailing on enactment: see above and *Attorney-General v Williams* [1990] 1 NZLR 646.

Such an approach is clearly not without its dangers; vast quantities of materials may be thought to be relevant and lawyers who argue the case will be venturing into disciplines in which they have no formal training. We should perhaps learn from the mistakes of one of the greatest scientific minds of the twentieth century, Linus Pauling, a double Nobel laureate, who cut such a tragic figure when he entered the field of medical biochemistry from the closely related discipline of pure chemistry.

Perhaps the most famous example of a New Zealand Court taking extraneous matter into account is *Z v Z* [1997] 2 NZLR 238 where the Court of Appeal, concerned at the possible consequences of their decision in a matrimonial property case, appointed as amici curiae counsel for a pressure group, and following representations allowed counsel for two other pressure groups to appear. The subsequent Court case seemed closer in spirit and procedure to a general inquiry rather than to a Court case deciding an issue between plaintiff and defendant. The judgment of the Court referred to sociological and economic factors, but has been subject to criticism both on the grounds of the procedure adopted and on the quality of the economic reasoning adopted by the Court: see Robertson [1997] NZLJ 38. Indeed Robertson goes so far as to state that the judgment in *Z v Z* "is pervaded by elementary economic fallacies".

It may well be that Parliament wishes to limit the Courts' use of such materials. Certainly the omission of the word "context" from s 5(1) of the Interpretation Act 1999 was deliberate and in opposition to the advice of both the Law Commission and the Law Society. Such a deliberate act must have a purpose, especially when one considers the reason for this decision, namely "The word 'context' was omitted from the Bill [and the Act] because it is imprecise and its inclusion may widen the Courts' current approach to interpretation".

Again it is suggested that Parliament fears that the Courts are usurping the legislative function.

A topic that is related to context in its wide sense is the use of the parliamentary history of an Act. The Courts in New Zealand, like those in England and Australia, have traditionally taken a restrictive attitude to the use of such materials as *Hansard* or reports recommending changes to the law, using these materials only to ascertain the mischief the statute was intended to remedy.

The dangers of using such materials are obvious: Parliament may well have intended different changes from those recommended by law reform bodies in their reports, and the quality of parliamentary debates and speeches can vary widely. Nevertheless, over the last fifteen or so years the Courts have exercised a discretion to consider the parliamentary history of a Bill. Thus parliamentary changes to a Bill during its passage through Parliament have been referred to: *Brown & Doherty v Whangarei County Council* [1990] 2 NZLR 63 as well as parliamentary debates: *Marac Life Insurance Ltd v Commission of Inland Revenue* [1980] 1 NZLR 694 being perhaps the most important of the earlier cases showing the use of this discretion. It is interesting to note that when the exclusionary rule was relaxed in England in *Pepper v Hart* [1993] AC 593, the Court discussed the arguments both for and against and placed careful limitations on the new relaxed rule. In New Zealand the rule has been relaxed without any detailed explanation or limitation.

However, the Courts have held that these aids to interpretation cannot be used to alter the meaning of a statute which is clear as enacted; see eg *R v Howard* [1987] 1 NZLR 353; *Tautau v Ministry of Transport* [1991] 2 NZLR 204.But the Courts have left open the question as to whether general words in a statute can be held to have a restricted meaning after consideration of these extra-statutory sources; *New Zealand Maori Council v Attorney-General* [1987] 1 NZLR 641.

It would also seem from recent cases that the New Zealand Courts are applying an approach similar to that in *Pepper v Hart* and are not relying on records of parliamentary debates unless the legislation is ambiguous or obscure or leads to an absurd result. Indeed the New Zealand Court of Appeal has stated that "it would not wish to encourage reference to such materials, except in the exceptional case"; *Wellington International Airport Ltd v Air New Zealand* [1993] 1 NZLR 671

In the context of parliamentary history it is interesting to note that in its submissions to the Justice and Law Reform Committee, the New Zealand Law Librarians Group sug-

gested that Acts of Parliament should contain a "legislative history" at the end of every printed statute. This legislative history would be a summary of an Act's historical process through Parliament and would have included titles, numbers and dates of all relevant Bills, details of any Supplementary Order Papers and the dates of all assent copies. It could also include references to *Hansard*, relevant treaties, law reform publications and any printed reports on the Bill.

This suggestion was rejected on the grounds that if such a legislative history were to be included then by s 5(2) of the Interpretation Act 1999 it could be used as an aid to interpretation and could lead to uncertainty in interpretation.

As this is currently one of the interpretative tools used by the Courts this statement appears to denote some hostility on the part of Parliament to the use of non-statutory aids to interpretation. In this context we could perhaps note that Parliament has extended those parts of a statute that may be used in ascertaining the meaning of the statute. Thus s 5(f) and s 5(g) of the Acts Interpretation Act 1924 provided;

> 5(f) The division of any Act into parts, titles, divisions, or subdivisions, and the headings of any such parts, titles, divisions, or subdivisions, shall be deemed for the purposes of reference to be part of the Act, but the said headings shall not affect the interpretation of the Act:
>
> 5(g) Marginal notes to an Act shall not be deemed to be part of such Act:

However, the corresponding provisions in the Interpretation Act 1999, namely s 5(2) and s 5(3) state:

> 5(2) The matters that may be considered in ascertaining the meaning of an enactment include the indications provided in the enactment.
>
> 5(3) Examples of those indications are preambles, the analysis, a table of contents, headings to Parts and sections, marginal notes, diagrams, graphics, examples and explanatory material, and the organisation and format of the enactment.

Thus marginal notes and the structure of the Act may be used in interpretation.

This change could be viewed as reflecting more accurate modern drafting techniques, or as a direction to the Court to rely more on the actual content of the statute in question in interpretation matters.

In retrospect, the New Zealand Bill of Rights Act 1990 may be seen as a rehearsal of the current conflict. The Bill of Rights, as originally proposed in the 1985 White Paper was a "strong" Bill in several respects. Firstly it would have given the Courts power to declare legislation which contravened the Bill void; secondly its provisions would have been entrenched and not capable of repeal by a simple majority in Parliament; finally it would have contained remedies for its breach.

However, in what may, with the benefit of hindsight, be seen as the clear beginnings of a constitutional clash between Parliament and the Courts, the Justice and Law Reform Committee recommended that these provisions be not enacted and Parliament accepted the recommendations. Thus the final Bill of Rights Act 1990 is an ordinary unentrenched statute that does not give the Courts power to declare any other legislation invalid or to decline to apply any other legislative provisions (see s 4 of the 1990 Act).

The reason the Committee advanced for this change (and presumably the reason that Parliament accepted the recommended changes) was that it had found concern among the public at the new additional powers the original Bill would have conferred on the Courts and "the redistribution of power .... from elected representatives of the people who were directly accountable to them to the judiciary who were appointed and held office until their retirement" (see the Final Report of the Justice and Law Reform Committee on a Bill of Rights 1988).

As is typical of most Bills of Rights the rights and freedoms are often expressed as general principles, eg s 16 and s 17. In those circumstances it is not possible for the Courts to apply a strict literal meaning, and it has never been argued that anything other that the purposive approach is correct. This approach had led to a judicial addition to the Bill of Rights Act 1990 in that the Court has held that the Bill requires a remedy in damages for its breach: *Simpson v Attorney-General (Baigent's Case)* [1994] 3 NZLR 667.

It might be thought that the absence of a remedy in the Bill of Rights Act was a deliberate action by Parliament, especially since the draft Bill proposed in the White Paper included such a remedy. However, the Court of Appeal attached little weight to this stating that "the Act requires development of the law when necessary".

In addition the Court relied on an Explanatory Note to the Bill which later became the 1990 Act and statements in Parliament to the effect that the Courts might enforce the rights contained in the Bill in different ways in different circumstances. It might be suggested by more cynical observers that the Court was happy to use extra-statutory material when it conferred a wide discretion on the Court but was not willing to use extra-statutory material which cut down its discretion.

Finally, let us consider some statements from the report of the Justice and Law Reform Committee on the Interpretation Act 1999:

- the word "context" was omitted from the Bill because it is imprecise and its inclusion may widen the Courts' current approach to interpretation;
- the main rationale behind [s 5] is to ensure that the Courts, in accordance with their constitutional role, give effect to the law as expressed by Parliament;
- a direction to take "context" into account may lead to a more liberal approach to statutory interpretation that departs from the words of the statute and therefore the purpose of Parliament;
- a legislative history, if included, may be used as an aid to interpretation, which could lead to uncertainty in the interpretation of legislation.

It is submitted in conclusion that the overall effect of the Interpretation Act 1999, particularly in view of the changes made by the Justice and Law Reform Committee and accepted by Parliament, is that Parliament does think that some of its law making functions have, in the past, been usurped by the Courts and that the 1999 Act represents an attempt to rein in this tendency of the Courts. The question is whether the Act will have any effect in this direction. Professor Burrows in the recent second edition of his excellent and authoritative text *Statute Law in New Zealand* is of the opinion that the Act will make little difference. Perhaps the answer is that when the Courts want to reinforce their reasoning they will quote extra-statutory material, but when such material conflicts with their reasoning they will ignore that material as the Court of Appeal seemed happy to do in *Baigent*'s case. ❑

MORE CENSORSHIP, DISCRIMINATION AND BILL OF RIGHTS

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examines the Court of Appeal decision in Living Word

The Court of Appeal has clarified some important aspects of the relationship between censorship, human rights and fundamental rights. In *Living Word Distributors Ltd v Human Rights Action Group (Wellington)*, the Court found ([2000] 3 NZLR 570), that the High Court had erred in law in upholding a decision of the Film and Literature Board of Review which effectively banned two videos discussing the rights of homosexuals in a negative context, HC Wellington, 1 March 2000, AP 26/98 Durie and Heron JJ; see Cheer [2000] NZLJ 244. The judgment reflects a desire to maintain clear distinctions between New Zealand's censorship legislation (the Films, Videos and Publications Classification Act 1993 – "the 1993 Act"), and its anti-discrimination legislation (the Human Rights Act 1993 – "the Human Rights Act"), but also to ensure that the rights in the New Zealand Bill of Rights Act 1990 ("the Bill of Rights") permeate the censorship regime.

THE VIDEOS

The two videos, both made in the USA in 1989, discussed homosexuality, and have not faced censorship challenges in other jurisdictions. One, called *Gay Rights/Special Rights Inside the Homosexual Agenda*, presented a view which opposed the pursuit of equal rights by groups of gay, lesbian, bisexual and transgendered people. The other, entitled *AIDS: What You Haven't Been Told*, presented a view that homosexuality is the cause of HIV and AIDS. The videos were originally labelled R16 by the Film and Video Labelling Body, but were then referred to the Films, Videos and Publications Classification Office by the Human Rights Action Group. The Office classified them R18, reasoning that the gay and lesbian community could well defend itself against attack, but that the content of the videos required a mature audience. The Board of Review replaced this classification with one of objectionability which was upheld by the Full Court of the High Court. Living Word appealed the decision to the Court of Appeal, arguing there had been an error of law.

The appellant made three main arguments to establish error: that the videos did not fall within the jurisdiction of the classification regime; that the Bill of Rights had not been applied correctly, and that the view the Board of Review had taken of the content of the videos was not one which was reasonably open to it. The Court found for the appellant on the basis of the second argument and remitted the matter back to the Board. Thomas J also found for the appellant but would have quashed the Board's decision without more.

THE MAJORITY REASONING

The jurisdictional argument was resolved as a matter of statutory interpretation. To fall within the classification jurisdiction, the videos had to be publications which fell under s 3(1) of the Films Act. It provides:

> a publication is objectionable if it describes, depicts, expresses, or otherwise deals with matters such as sex, horror, crime, cruelty, or violence in such a manner that the availability of the publication is likely to be injurious to the public good.

The High Court had found that although the videos focused on a perceived homosexual agenda, nonetheless homosexual sex was dealt with in part. This part would do to found jurisdiction. But the High Court acknowledged that the videos dealt with sexual orientation in the main, and therefore also considered whether this topic could be a "matter such as sex, horror, crime, cruelty or violence". It found the approach in the statute to be a general one and the list open-ended, which could therefore include the topic of sexual orientation. The Court of Appeal firmly rejected this approach. It held that s 3(1) had two purposes: to define the subject matter covered by the Act, and to describe the character of that subject matter (as being injurious to the public good: para 25). The subject matter was limited by reference to the list (sex, horror etc) because those words established a class of relevant publication, and although the words "such as" allowed other examples, these would have to be of the same kind as the class established in the statute. Furthermore, the words used in the class pointed to activity rather than expression of opinion (paras 26-28).

This interpretation also determined the meaning of s 3(3)(e) of the 1993 Act (requiring that particular weight be given to the manner and extent to which a publication "[r]epresents ... that members of any particular class of the public are inherently inferior to other members of the public by reason of any characteristic of members of that class, being a characteristic that is a prohibited ground of discrimination specified in s 21(1) of the Human Rights Act 1993"). It did not create a special stand alone topic for censorship which could embrace the videos. It merely pointed to factors

which may be given weight in the censorship process. Therefore if a publication dealing with sex, horror, etc ... (ie: one which has passed through the "subject matter gateway" of s 3(1)), represented that members of a particular class of the public are inherently inferior by reason of a characteristic which is a ground of discrimination under the Human Rights Act, particular weight would be given to that feature of the publication but no more (paras 31-33).

Videos about sexual orientation did not get through the subject matter gateway, because they did not have the relevant content to attract regulation (paras 24-29). However, the Court noted the videos might deal with "matters such as sex" (para 34). It appears from the judgment that these Judges did not actually view the videos (although Thomas J clearly did). They were therefore not prepared to examine this point any further, being content to leave it for the Board when the case was remitted to it.

On the Bill of Rights argument, the Court once again referred to *Moonen v Film & Literature Board of Review* [2000] NZLJ 145, and rejected the argument that the interrelationship of the Bill and the censorship legislation in this case produced a clash between freedom of expression and freedom from discrimination in which the latter trumped the former. First, it confirmed that the Bill of Rights is always engaged in the censorship process because the censorship bodies perform public functions (para 37). The act of state censorship attracts the operation of the Bill. Next, the Court noted it had applied s 6 of the Bill of Rights and construed the requirement of likely injury to the public good in s 3(1) of the 1993 Act in a way which was in harmony with the Bill by stating it applied to depictions of activity rather than opinion. This also provided a reasonable limit as could be demonstrably justified in a free and democratic society (s 5 of the Bill) (para 39).

But more importantly, the Court held that interpreting s 3(1) required freedom of expression to be given full weight in assessing whether the videos were likely to injure the public good. The right to be free from discrimination was not directly relevant at that point, but the values underlying it could be imported and become a particular consideration via s 3(3)(e) if the subject matter is right (para 40). This was not a direct clash between rights. The fundamental test was to balance the right of speakers and the public to receive information under s 14 of the Bill against a state interest in protecting citizens from harm caused by speech. The High Court had not done this.

In remitting this issue to the Board of Review to begin afresh, the Court of Appeal appended an ode to freedom of expression, quoting from the House of Lords in *R v Secretary of State for the Home Dept, ex p Simms* [1999] 3 All ER 400, and the European Court of Human Rights in *Handside v UK* (1976) 1 EHRR 737, which refer to the importance of the freedom to engage in informed political debate, and the demands of pluralism, tolerance and broadmindedness which infuse a democratic society (para 45). The Board would obviously need to assess whether the focus of the videos was on the expression of political and social opinion (para 44) with these hints in mind.

In the light of these conclusions, the Court did not see a need to determine the issue whether the High Court erred in holding that the Board's interpretation of the content of the videos was one which was reasonably open to it. However, it noted in obiter statements a possible argument that the High Court had reached its finding on that issue applying an incorrect interpretation of s 3(1) as to the necessary injury to the public good (paras 46-50).

THOMAS J

In a separate judgment, Thomas J made it clear that he had viewed the videos and would not remit them to the Board of Review, but would quash the Board's decision. The Judge described the content of the videos in some detail (paras 54-67) and concluded they portrayed the beliefs and prejudices of religious fundamentalism. He then delivered a strong caveat indicating that he neither supported nor condoned the content of the material – rather, his opinion was irrelevant to the matter of censorship. Thomas J surveyed the history of the censorship legislation and concluded it is not directed to preventing discrimination. The Judge generally endorsed the approach of his fellows, in particular that under *Moonen*, freedom of expression was a necessary consideration where a provision in the 1993 Act is capable of more than one meaning (para 77). However, he went further and held all the rights in the Bill of Rights should be relevant to the censorship question unless precluded by the statute and the right to be free from discrimination could even be directly relevant. But because the 1993 Act deals with censorship, freedom of expression would tend to be "particularly germane" (para 78). In the context of the Act it could not override or outweigh the express matters in s 3(3) to be given weight and s 3(4) to be considered, but it was always a relevant consideration under s 3(1) (para 79).

On the jurisdiction point, Thomas J was not prepared to remit the issue back to the Board. His view was that the Board had exceeded its jurisdiction in dealing with the videos. They did not fall within s 3(1) because they did not describe, depict, express or otherwise deal with sex or a matter such as sex. Any references to homosexual sex were a minute fraction of the total footage and could have been dealt with by excision. Sex in the Act meant pornographic sex (the Judge did not define "pornographic") and not discrimination based on sex. He concluded the videos were essentially political tracts (paras 81-82).

Thomas J sought a "nexus between the subject matter and injuriousness" requirements in s 3(1) of the 1993 Act (para 80). However, he found that in *Living Word* there could be no connection made by the Board between the subject matter of the videos and the supposed injury to the public good. Videos treating the topic of homosexuality in an abhorrent way might have a harmful effect, but did not have the right content. The inability to make such a link between content and injury was decisive (paras 80-86). This approach was essential because otherwise ... "Political, religious or other opinions which should have unrestricted dissemination in a free and open society would be at risk of being banned if they were expressed in a publication which also dealt, perhaps peripherally, with sex or violence" (para 87).

Comment

The reasoning used by the Judges to establish a subject matter gateway is not entirely robust. The use of the words "such as" followed by a list are indeed "both expanding and limiting" (para 27), in that "such as" is more restrictive than the alternative "includes", while still maintaining an element of open-endedness. The Court concluded other matters could fall within this part of s 3(1), but they had to be of the same kind as used in the list because the list contained examples of a class. But the words used in the 1993 Act do not clearly form a class. Sex, horror, crime, cruelty or

violence do not share obvious features, unless one wishes to argue that they are all harmful ie: are likely to injure the public good. Cruelty, crime and violence clearly do – they carry their negativity on their face as part of their meaning and are perceived immediately in such a fashion. However, sex is not in this category and is arguably the opposite. Horror is a chimera, but part of the difficulty of attaching meaning to the word horror is that it does not tend to point to activity, as suggested by the Court (para 28). Horror is generally an expression of human emotion, which may not be seen in a negative way, but rather, as exciting – some of us love to be horrified. The word is intended in the legislation to capture a particular genre of depiction which arose in comics and films. But a horror publication is not in itself inherently harmful – indeed, some are harmless and good fun and others are accepted as works of great art or literature. Therefore it cannot be said that the words in the list clearly form a class, or that they all tend to point to activity, rather than opinion.

It would be more accurate to describe the list as containing separate and reasonably disparate subject headings. To enter the subject matter gateway, a publication must fall under one or more heading. The Court recognised this possibility when it describes the list as establishing "five categories" (para 27), but a list of five categories does not establish a class. The Court denied that what is required is a bare focus on the categories specified. With respect, that is exactly what is required and what the effect of *Living Word* must be. The list is closed in that there can be no other categories, but open in that each category heading establishes a separate class into which material must fall.

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In spite of this, one can generally see what the Court was getting at. However, the decision renders wrong in part the recent reclassification decision by the Board of Review in *Moonen*, decision 8 September 2000 (see Cheer [2000] NZLJ 145), a decision released after *Living Word*. In it the Board reclassified all material previously considered using the Bill of Rights approach suggested by the Court of Appeal decision in the same case and supplying detailed reasons. Two photos which were objectionable are now unrestricted, but otherwise all the classifications remain the same. The Board surprisingly adopted the position it had already taken in its previous decision to the interpretation of s 3(1). It stated: "It does not exclude consideration of other matters. ... those other matters are, however, qualified by the final phrase 'injurious to the public good'. ... regardless of whether or not these publications deal with matters of sex, horror, crime, cruelty or violence, they can be brought into the definition of 'objectionable' and made subject to the Board's jurisdiction by the words 'such as'" (at p 16). The Board had used identical wording in *Living Word*, to which the Court of Appeal responded "If it were intended that 'matters' should extend to 'all matters', there would be no need for the expression 'such as' and no sense in it" (para 30).

The conclusion of the Court in *Living Word* that the categories in s 3(1) tend to point to activity rather than the expression of opinion or attitude (paras 28 and 39), could have surprising potential to reduce the ambit of the classification regime if taken to its fullest conclusion. As noted above, arguably not all of the categories in the section obviously deal with activity in any event, but the approach misconceives the nature of censorship. One can see clearly that the Court was seeking to bolster its view that the classification legislation should be about censoring depictions of really harmful and naughty stuff (ie: people having sex or doing violence), not genuine opinion, and the human rights legislation should deal with discrimination and censoring opinion in a very limited context, if at all. But our classification officers regularly deal with material which does not show activity. The *Moonen* case itself dealt with photographs of nude children not engaged in any sexual activity, but depicted in a sexual manner due to the focus on genitalia. These were dealt with under ss 3(1) and 3(3)(b) of the 1993 Act as exploiting the nudity of children. Further, photographs of dead and mutilated bodies show the results of activity but are mere depictions of those results. Robert Mapplethorpe's photographs of mutilated genitalia show the results of sado-masochistic activity, but not the activity itself. A video or recording of a person describing a violent rape is about a past act, but does not show the act itself. Classic books such as *Lolita*, or *120 Days of Sodom* may contain some descriptions of sexual or violent activity, but express world views when taken as a whole.

But more than this, the very basis of censorship, which is enshrined and emphasised in s 3(2) of the 1993 Act, and implied in the remainder of s 3, is a judgment about what is harmful whether it be opinion or activity. Under s 3(2), specified publications are seen as harmful if they promote or support, or tend to promote or support, harmful activity. So the question asked when the Classification Office dealt with two Robert Mapplethorpe photographs depicting urolagnia and sado-masochism was whether the photographs tended to promote or support the activities (OFLC Refs 9501765 – 67). The question asked when *New Truth* published advertisements for services and videos involving urolagnia and sex with young persons was whether the newspaper promoted or supported the activities by running the advertisements (*News Media Ltd v Film and Literature Board of Review* (1997) 4 HRNZ 410). Promoting or supporting, or tending to promote or support, something is expressing an opinion about it. It would be strange if s 3(2) could apply to opinion while the balance of the provision could not. However, publications which qualify under the other parts of s 3 are also injurious if they show harmful activities in a positive light, which again, may involve expressing an opinion. For example, if material positively supports criminal activity, such as the cultivation of marijuana, it is banned (OFLC Ref 9801335), but if it also has a political message, such as the reform of marijuana laws, it may be merely restricted (Decision 1/98 of the Board of Review).

Finally, to attract the protections the Bill of Rights gives to freedom of expression, publications which come under the censorship regime must be seen as at least forms of expression, not just depictions of activity. I have dealt with this issue elsewhere (Cheer, (1996) 6 Canta LR 324, 356-357), and merely note here that Canadian jurisprudence (*R v Butler*, (1992) 89 DLR (4th) 449, 472) and the previous indecent publications regime in New Zealand (*Re Penthouse (US) Vol 19, No 5 and others* [1991] NZAR 289), accepted

that even material depicting sexually explicit activity, for example, is a form of expression which conveys ideas, opinions or feelings.

Any attempt to suggest the 1993 Act does not, or is not intended to, draw the expression of ideas or opinions into its net is oversimplified. The Court used the approach to construe likely injury to the public good in s 3(1) and saw itself as complying with ss 5 and 6 of the Bill in doing so (para 39). Yet it seems extremely unlikely the Court intended that the examples given above should not have been classified at all, although this would please libertarians. Although the actual result in *Living Word* is desirable, general statements of this sort may give rise to much detailed argument in the future about whether a publication depicts activity or expresses an opinion. A better approach might have been to hold that the 1993 Act did not apply to particular sorts of opinion (discussion of sexual orientation) and to emphasise when it does apply to political opinion, freedom of expression should be given great weight.

There will be little point in parties submitting material for classification containing s 3(1) subject matter which cannot be argued as injuring the public good. But nothing will be certain where there is a small amount of qualifying material, surrounded by other subject matter, as in *Living Word*. Logically, the smaller the proportion of material to the whole of the publication, the less likely there will be such injury. Suppose the Board on remission finds that there is a small proportion of material dealing with sex in the videos. It will have difficulty finding the nexus between this and likely injury to public good, but not necessarily on the same grounds as Thomas J. The reason is that in interpreting s 3(1) the Board must apply s 3(4)(a) which requires the dominant effect of the publication as a whole to be considered. This, combined with the requirement to take freedom of expression into account, would in most cases render nugatory any possible injurious effect. The content of any small proportion would need to be particularly invidious to cancel out such effect. Even if the nexus was made out for particularly obnoxious material, as noted by Thomas J, the adequate response would still be excision or an age restriction, rather than a complete ban on the entire publication. A Bill of Rights approach would suggest this also.

As to the Bill of Rights analysis, it is pleasing that the legislation has been interpreted in such a way that rights do not clash. Any other approach was unworkable, since, as all Judges note, freedom of expression must always feature in the censorship process. The judgments implicitly (and in the case of Thomas J, explicitly) elevate the place of freedom of expression in the censorship process above other human rights, which can only inform the process further. The multiple judgment gives very strong direction to the Board as to the value it should attach to the videos as speech if the focus is found to be on expressing political and social opinion. This also implies that if a small part of the video does not have such a focus it need not infect the rest.

Yet some of the dicta is confusing. The Court speaks of the need to give freedom of expression "full weight in the application of s 3(1)" (para 40). However, the values underlying rights in the Human Rights Act such as freedom from discrimination, can be "imported and become particular considerations". Although the Court made it clear this does not involve a clash of rights, it is all rather vague. What are values underlying human rights? Are they less important or more important than the rights themselves? How is particular consideration to be given to such values? Although freedom of expression must be given full weight, human rights values (but not the rights themselves) may be directly relevant and must be given due consideration. It seems entirely possible that a particular consideration could be a deciding factor once freedom of expression has been given full weight. This might well look like one right trumping another. The judgment of Thomas J is also not particularly helpful on this issue. The Judge concluded that all the rights in the Bill should always be a relevant consideration (directly or indirectly) in the censorship process, including the right to be free from discrimination. Although he went on to state that freedom of expression will be particularly germane, the dicta implies a direct clash of rights is possible (para 78). This issue remains unresolved – there is a lack of guidance as to how a direct clash of two rights in the Bill should be resolved in the context of censorship.

The Judges in the main judgment stated that "[T]he ultimate inquiry under s 3 involves balancing the rights of a speaker and of the members of the public to receive information under s 14 of the Bill of Rights as against the state interest under the 1993 Act in protecting individuals from harm caused by the speech" (para 41). This does not explicate a practical test – it merely tells us what we already know – that the process is a balancing one. But Thomas J would not have allowed freedom of expression to permeate the whole censorship regime. He concluded that if a publication promotes or supports, or tends to promote or support, the matters contained in s 3(2), it must be deemed objectionable and freedom of expression can have no bearing on the issue (para 79). This is not in accordance with the Court of Appeal decision in *Moonen*. There the Court held that any interpretation of the "promotes or supports" test in s 3(2) had to impinge on freedom of expression as little as possible (at paras 16-19, 23). However, Thomas J's approach is shared by the Board of Review. In the decision reclassifying the *Moonen* materials, it went so far as to say it "would ... have been prepared to designate child pornography as outside the protection of s 14 altogether ... (at p 13) and in the absence of the Court of Appeal's decision in *Moonen*, [it would have] inclined to the view that the freedom of expression guaranteed by the Bill ... was not engaged in this case, in so far as child pornography is not protected speech. ... the Court may wish to reconsider its views on this topic in due course" (at p 24). This extraordinary view was shared by the previous Chief Censor, and is based on a notion that child pornography can be easily identified and defined. However, the Board did not find that the need to take account of freedom of expression prevented it from reaffirming its previous classification of all material in *Moonen*, except for two photographs.

Moonen in the Court of Appeal had become the leading Bill of Rights case in New Zealand. In censorship matters, it requires sound reasons to be given whenever our censors wish to prevent adults ever seeing certain publications. This is as it should be. *Living Word* emphasises the importance of freedom of expression in the process of censorship and gives a rather vague place to values underlying human rights in relevant cases. Most importantly, it clarifies the limited categories of material to which the 1993 Act can apply outside s 3(2) and makes clear the requirement of a connection between such categories and likely injury to the public good. However, in the process, it may have raised the spectre of increased litigation on the distinction between banned activity, and opinion. ❑

JUDICIAL TRENDS IN TAXATION

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finds the attitudes of the Courts to the definition of income changing

This article focuses on recent New Zealand judicial trends in the area of taxation. There has already been considerable commentary on a number of the cases discussed below and this article is not intended to discuss the cases in detail. The focus will be more on the approach that the Courts have taken and the main themes appearing in the context of the capital/revenue distinction, tax avoidance and principles of statutory interpretation.

CAPITAL/REVENUE DISTINCTION

The capital/revenue distinction is one of the most notoriously difficult areas of income tax. Judges have suggested that the outcome in any particular case could be determined by the spin of a coin, that the issue is an "insoluble conundrum" and that it is an intellectual minefield in which the principles are illusive and analogies treacherous.

A useful starting guide is the observation of Lord Pearce in *BP Australia Ltd v FCT* [1966] AC 224, approved by Richardson J (as he then was) in *CIR v Thomas Borthwick & Sons (Australasia) Ltd* (1992) 14 NZTC 9,101 as exemplifying the "governing approach" in New Zealand:

> The solution to the problem is not to be found by any rigid test or description. It has to be derived from many aspects of the whole set of circumstances some of which may point in one direction, some in the other. One consideration may point so clearly that it dominates other and vaguer indications in the contrary direction. It is a commonsense appreciation of all the guiding features which must provide the ultimate answer. Although the categories of capital and income expenditure are distinct and easily ascertainable in obvious cases that lie far from the boundary, the line of distinction is often hard to draw in border line cases; and conflicting considerations may produce a situation where the answer turns on questions of emphasis and degree. (at 264.)

Another test looks at what "the expenditure is calculated to effect from a practical and business point of view rather than upon the juristic classification of the legal rights" (per Dixon J in *Hallstroms Pty Ltd v FCT* (1946) 8 ATD 190). The *Hallstroms* principle has been approved in New Zealand (see in particular *Thomas Borthwick* (CA) and *Wattie v CIR* [1999] 1 NZLR 529 (PC)). A number of other tests have been developed to assist the overall analysis including: the need or occasion for the payment; the enduring benefit test; how the payment would be treated on ordinary principles of commercial accounting; and whether the amount is referable to the business structure (capital) or to the process by which income is earned (revenue).

Forest Research Institute

In *CIR v New Zealand Forest Research Institute Ltd* [2000] 3 NZLR 1, the taxpayer agreed to acquire the assets and undertaking of a business. As part of the consideration for the acquisition of a business, it agreed to take over certain liabilities, including certain of the vendor's contractual obligations to its employees (vested or contingent entitlements to leave). The Privy Council held that the subsequent payment of these sums was capital and not deductible, being part of what was paid for the acquisition of the assets. The Privy Council rejected the argument that the expenditure should be deductible on the basis that the contract of employment was "unbroken" as provided by s 41 of the Crown Research Institutes Act 1992.

Auckland Gas

Auckland Gas Co Ltd v CIR [2000] 3 NZLR 6 concerned the deductibility of expenditure incurred by Auckland Gas on its low pressure gas distribution pipeline system for five income years. The High Court held that the relevant expenditure was deductible whereas the Court of Appeal held that it was capital. The expenditure was designed to address two major problems, gas leakages and entry of water. Auckland Gas adopted the technique of inserting polyethylene pipes into the existing cast iron mains and steel services. This actually reduced the volumetric capacity of the system, but allowed gas to be transmitted at a much higher pressure than previously. The issue was whether the relevant expenditure was "repairs" (deductible) or "replacement" (not deductible). The Privy Council held that the expenditure involved a replacement.

The judgment of the Privy Council was brief. The following three-fold analysis was adopted:

(a) the first step is to identify the object to which the test of repair or replacement is being applied – in difficult cases questions of degree will arise;

(b) the effect of the work on the character of the object is an important consideration. The main issue here is whether the character of the object has changed as a result of the expenditure;

(c) finally, there is no rigid test or description that can be applied and the answer depends upon a consideration of all the circumstances.

Having regard to the facts, the Privy Council held that there was a replacement because the new pipes differed from the old as they were virtually leak free; they were much better suited to the passage of dry and clean natural gas; and they carried gas at a higher pressure. In addition, substantial

portions of the cast iron mains and steel services were superseded by the polyethylene pipes having the differences/advantages mentioned.

Importantly, the Privy Council was again prepared to embrace the principles expounded by Lord Pearce in *BP Australia* and Dixon J in *Hallstroms*.

Birkdale Service Station

Birkdale Service Station Ltd v CIR (1999) 19 NZTC 15,493 involved Mobil Oil making payments referred to as inducement (or compensation) payments to petrol retailers in consideration for which the retailers undertook to sell only Mobil products. Based on the nature of the arrangements, Laurenson J held that the receipts were taxable in the hands of the retailers.

In my view, this is probably one of the more difficult recent cases concerning the capital/revenue distinction. The judgment in this case is long (in contrast to more recent Privy Council cases) and contains a close analysis of the formal nature of the arrangements as well as an extensive review of the capital/revenue authorities.

The inducement payments were seen to be linked to the income producing process of the retailers through the petrol quota system. That is, the terms of the agreement provided for a quota of product to be purchased by the retailer and there was a provision for the payment of liquidated damages in the event of a breach of the supply agreement by the retailer. In some of the transactions, the compensation payments were documented as a loan. Laurenson J reasoned that at the point when a litre of product was sold the retailers made a gain, being a reduction in the contingent liability to meet liquidated damages. Those gains were seen to be derived from their business in the sense that they were directly referable to the process by which they operated to obtain regular returns.

It is submitted that it is entirely possible that the receipts could have been held to be capital. Some observations follow:

- one of the difficulties is the holding that there was a gain when a litre of product was sold (being the reduction in the contingent liability to meet liquidated damages). A key principle of income tax law is that *income* is something that comes in and not what is saved from going out. Therefore, it is respectfully submitted that an appropriate approach may have been to characterise the nature of the inducement receipt itself and not focus on what happened after it was received;
- on one view, the relevant receipts were referable to the business structure of the retailers and such receipts provided an enduring benefit to their business. The High Court did not see the receipts in this light and essentially regarded them as prepayments of income;
- at a broad level, it is possible to look at the inducement receipt in *Birkdale* as being no different to the lease inducement in *Wattie* (see below). From a "practical and business point of view" both receipts can be seen as referable to the business structure (ie capital). As the Privy Council observed in *Wattie* the crucial question is whether in all the circumstances the receipt can properly be attributed to a particular year – it is submitted that it may not have been possible to attribute all the receipts to the year in which they were paid;
- the holding in *Birkdale* differs from a number of cases in this area which have held that receipts of a similar nature are not taxable. As discussed in the case, the conclusion was also contrary to Inland Revenue's stated policy on the issue contained in Public Information Bulletin 178. On the facts, Laurenson J was able to distinguish cases such as *CIR v Dunlop's (Wanganui) Ltd* [1970] NZLR 1125 (informal trade tie receipt from Mobil not taxable); *CIR v City Motor Service Ltd*; *CIR v Napier Motors Ltd* [1969] NZLR 1010 (payments by oil company to dealers for capital improvements, where trade ties were only implied, were held to be non-taxable receipts).

On 14 November 2000 the Court of Appeal gave judgment (CA 119/00 and CA 31/00), holding that the receipts in ten of the arrangements were taxable and that one receipt was not. The ten arrangements that were held to be taxable had terms varying between three and ten years and each arrangement consisted of a compensation agreement (which contained the "quota"), a retail supply contract and an equipment loan contract. The recitals of the compensation agreement noted that the funds were required to improve facilities and services and in order for the retailers to compete effectively. The essence of the retail supply contract was that the retailer should operate its business so as to promote and maximise the sale of Mobil products (in the event of default by the retailer Mobil was entitled to suspend deliveries). In one part of the judgment it was acknowledged that if the retailers wished to remain in business they had to accept the tie. In another part of the judgment it was observed that the manner of conducting the retailer's business may have changed, however, this was thought to relate to the revenue derivation process rather than an alteration to structure. With respect, there appeared to be a number of features that affected the business structure and provided enduring benefits, however, on the facts these were not regarded as decisive.

From a practical and business point of view, the payments had a "revenue" characterisation having regard to: the accounting treatment (revenue) which provided minor support but was not determinative; the fact that little freedom was actually surrendered by the retailers and that they had no real choice (in part, this is a finding specific to the New Zealand petrol retail industry); and the length of the trade ties (the initial ties varied between three to five years and this enabled other trade tie cases to be distinguished). The overall impression created by the facts was that in all but one case, the compensation was an incident of the carrying on of the business without any change of a structural nature. The Kenlock Motors arrangement, with a 15 year tie and effectively a security interest in the land and buildings to Mobil, was regarded as unique and was held to be capital.

The writer respectfully submits that there were sufficient features that, on balance, could have supported a capital characterisation. Arguably, the real effect of the "quotas" was that they were designed to increase efficiency and it is submitted that this, and other features, go to structure. If *income* is a "flow" and the pipe carrying that flow is *capital*, surely all that happened in *Birkdale* was that the pipe was structurally enlarged. At one level, it is difficult to reconcile *Birkdale* and *Wattie* (particularly having regard to the Court of Appeal's treatment in *Wattie* of *Myer* and the extraordinary receipts principle), however, the specific facts of *Birkdale* will probably be used to justify the different approach taken.

Wattie

Much has already been written about *CIR v Wattie* [1999] 1 NZLR 529. As most readers will be aware, the case concerned a lump sum lease inducement payment of $5 million from the lessor to the lessee (Coopers & Lybrand). The Privy Council held that the receipt was an affair of capital and was therefore not taxable in the hands of the lessee.

The main reasons for the receipt being regarded as capital were:

- from a practical and business point of view, the payment related to the acquisition of a capital asset and it brought into existence an asset or an advantage for the enduring benefit of a trade;
- the payment was akin to a "negative premium" (to apply an analogy with *CIR v McKenzies (NZ) Ltd* [1988] 2 NZLR 736);
- traditionally (and in the absence of special legislation) lease premiums have been regarded as "capital" in the law of New Zealand as in the law of the United Kingdom;
- in all the circumstances, the payment or the receipt could not properly be brought into the income tax reckoning for a particular year and, therefore, it could not be brought into reckoning at all.

In the course of its judgment the Privy Council approved the principles established in *Thomas Borthwick*, *Hallstroms* and *BP Australia*. There was also endorsement of the "enduring benefit" test formulated by Viscount Cave LC in *British Insulated and Helsby Cables Ltd v Atherton* [1926] AC 205.

The *Wattie* decision will, in my view, go down in New Zealand tax history as a great case. The main reason for this is that the Court fulfilled its responsibility by preserving the overall integrity of the tax system – that is, an item which was truly of a "capital" nature was not allowed to be taxed as "income". According to ordinary concepts, the relevant amount was not income or a "flow" of income stemming from capital, rather it was the very capital itself.

The importance of the decision cannot be stressed enough. The Privy Council was able to make its holding, despite the fact that highest Courts in other countries (such as Australia and Canada) have reached different conclusions on the same issue. In my view, this demonstrates the responsibility of the Courts in New Zealand to preserve the integrity of the tax system and to maintain traditional capital/revenue boundaries.

Recent proposals in relation to the treatment of restrictive covenants/exit inducements suggest that the traditional capital/revenue distinction can be eroded by legislation. These proposals raise conceptual and policy issues beyond the scope of this article.

TAX AVOIDANCE AND STATUTORY INTERPRETATION

A recurring theme in tax avoidance cases is the role or approach of Courts in interpreting tax legislation, including anti-avoidance provisions.

Miller v CIR

In *Miller v CIR* [1999] 1 NZLR 275, the Court of Appeal had to consider a complex series of transactions and one issue concerned the application of the general anti-avoidance provision ("GAP") in the Income Tax Act 1976 – s 99. In very broad terms, the relevant schemes in this case were described as a "tax loss utilisation scheme" and a "business improvement scheme". The two key effects of the schemes were the conversion of net profits of a trading company to capital (in the form of the share price payable to the former shareholders) and the artificial inclusion of the trading company in an existing tax loss group. The complex transactions were described by the lower Court as "a blatant tax avoidance scheme, elegant though its components may separately have been".

The taxpayer argued that the Commissioner was obliged to invoke a specific anti-avoidance provision in the grouping provisions (less disadvantageous for the taxpayer) over the GAP. This argument was rejected – the Commissioner can choose to re-construct under a GAP (*Challenge Corporation Ltd v CIR* [1986] 2 NZLR 513).

The observations of Blanchard J that I wish to comment on are set out at pp 300-301: [Emphasis added.]

> It takes but an instant, however, to see that what the scheme as a whole achieved ... was to convert the net profits of the trading company to a capital sum in the form of the share price payable to the former shareholders ... The shareholders did not really sell their business, for after the agreed (inflated) price had been paid they could buy the assets back for an amount equal to the liabilities plus a nominal, or relatively nominal sum, ... This demonstrates the *unreal nature of the arrangements from any commercial perspective*, and is an indication that the shareholders were not actually selling the business operation. *While the form of the arrangement is not a sham it cannot be described as resulting in a capital transaction* .... Nor was there truly a sale when the shareholders later surrendered the options. That was merely a device to generate more administration charges and thereby convert more income into capital. The sum paid in exchange for this surrender was extravagantly out of proportion to the worth of the options ...
>
> ... Section 99(3) gives the Commissioner a wide re-constructive power. He "may" have regard to the income which the person he is assessing would have or might be expected to have or would in all likelihood have received but for the scheme, *but the Commissioner is not inhibited from looking at the matter broadly* and making an assessment on the basis of the benefit directly or indirectly received by the taxpayer in question.

The above approach at first appears very broad indeed. However, it is submitted that the approach has a sound principled basis. One leading commentator has suggested that there is an element in the judgment which seems to have the flavour of the application of fiscal nullity. The main principle of fiscal nullity, a concept developed by the English Courts, is that any steps inserted in a related series of transactions which have no commercial or business purpose apart from the avoidance of tax can be disregarded as being irrelevant by the Revenue and the related transactions can be viewed as a whole (see *WT Ramsay v IRC* [1982] AC 300 and *Furniss v Dawson* [1984] AC 474). Fiscal nullity has been rejected in Australia and Canada, and New Zealand Courts have not expressly decided on the scope of the principle. In *Mills v Dowdall* [1983] NZLR 154, Cooke J appeared to suggest that the principle could apply in New Zealand. Although the theoretical possibility of fiscal nullity is open in New Zealand, it is unlikely to flourish fully (and may well be modified if it is adopted on any basis at all), especially in view of our revenue legislation containing a GAP and comments in the recent *BNZ Investments* case.

Comments on Blanchard J's judgment follow:

- "while the form of the arrangement is not a sham, it cannot be described as resulting in a capital transaction" – there are two themes here. First, New Zealand Courts adopt a form over substance approach (unless there is a "sham" or a GAP mandates a broader or different approach – *Mills v Dowdall*). Second, fanciful arrangements designed to convert what would otherwise be income into capital can be struck down under ordinary principles ie it is possible that *income* may be found to exist without resort to a GAP – under this approach the income would never be regarded as having been effectively converted to capital or, the sum could be argued to be income under ordinary concepts (which extends to sums that are not capital). Alternatively, the approach is justified under a GAP or specific anti-avoidance rule (together with any reconstructive power) because "avoidance of tax is constituted by the alteration of the incidence of tax and the conversion of an income receipt into a capital receipt" (per Hill J in *Davis v FCT* 89 ATC 4,377). In my view, a role of a Court in a case such as *Miller* involves an analysis of the composite transaction to ascertain whether the incidence of income has been altered or whether income has been derived (even if the form of the transaction suggests there is a capital sum). This is simply part of the construction process that Courts undertake and is supported by a number of provisions including s BB 3(1) of the Income Tax Act 1994 which confirms that a person affected by a tax avoidance arrangement may not have satisfied an obligation under the Act (one such obligation being to pay income tax on taxable income);
- the arrangements were described as blatant, artificial and commercially unreal – these descriptions, coupled with the observations that in reality the transactions did not result in a capital transaction, allowed the conclusion that tax avoidance was involved. This is not surprising, as in tax avoidance cases the transaction adopts some unusual or artificial form to frustrate the scheme and policy of the Act (even though it appears to be within the letter of the law). A circular flow of funds, the "interposition of a cooperative intermediary" and the ultimate preservation of the status quo are all planned actions that have been found in the past to be indicative of avoidance (see the Australian decisions of *Davis v FCT* and *Oakey Abattoir Pty Ltd v FCT* 84 ATC 4,718). The arrangements were described as blatant, artificial and commercially unreal – these descriptions, coupled with the observations that in reality the transactions did not result in a capital transaction, allowed the conclusion that tax avoidance was involved. This is not surprising, as in tax avoidance cases the transaction adopts some unusual or artificial form to frustrate the scheme and policy of the Act (even though it appears to be within the letter of the law). A circular flow of funds, the "interposition of a co-operative intermediary" and the ultimate preservation of the status quo are all planned actions that have been found in the past to be indicative of avoidance (see the Australian decisions of *Davis v FCT* and *Oakey Abattoir Pty Ltd v FCT* 84 ATC 4,718). Recent New Zealand cases have highlighted that tax avoidance involves infringement of a norm of "impropriety" (see Baragwanath J in *Miller v CIR*; *McDougall v CIR* (1997) 18 NZTC 13,001). It does need to be noted that Woodhouse P in *Challenge* observed that a GAP (s 99) is not concerned with outright impropriety. Although the precise meaning of the concept of impropriety is unclear, mainly because it has not been fully developed by the Courts, it is submitted that its underlying rationale should be the defeat of the legislative scheme and policy. On this approach, another way of looking at *Miller* is to ask – did Parliament intend the purported tax benefits to be available, or is it *permissible* to obtain them?
- a GAP gives the Commissioner a wide reconstructive power – this has always been true of modern GAPs;
- "the Commissioner is not inhibited from looking at the matter broadly and making an assessment on the basis of the benefit directly or indirectly received by the taxpayer in question" – it is indeed true that the Commissioner can look at the matter broadly subject to the following important qualifications:
  - the Commissioner only has power to apply the terms of the statute to the form of the legal arrangement. As Richardson J said in *Mills v Dowdall*: "It is the legal character of the transaction that is actually entered into and the legal steps which are followed which are decisive. That requires consideration of the whole of the contractual arrangement and if the transaction is embodied in a series of inter-related agreements they must be considered together and one may be read to explain the others. In characterising the transaction regard is had to surrounding circumstances" (at 159);
  - in New Zealand, the above approach does not allow taxation by economic equivalence (see *Wattie*);
  - if the transaction is a "sham" the form of the transaction is ignored;
  - the Commissioner should only be entitled to reconstruct if the transactions are not genuine and the policy of the law is defeated – hence, a transaction that is not genuine and defeats the law's policy will bear the stamp of "tax avoidance". As Richardson J observed in *Mills v Dowdall*: "Commercial men are entitled to order their affairs to achieve legal and lawful results which they intend. If they deliberately enter into a *genuine transaction* intended to operate according to its tenor, those intentions should be recognised. It is what they choose to do that counts and their rights and obligations should be determined on that basis *except where the legislation has itself directed otherwise.*" (at 160.) [Emphasis added.]

In my view, it is possible to reconcile the judgment of Blanchard J with existing principles. It is understood that this case is being appealed to the Privy Council.

Hotdip Galvanisers

Hotdip Galvanisers (Christchurch) Ltd v CIR (1999) 19 NZTC 15,337 involved three companies that were grouped for tax purposes. The loss company went into receivership. The Commissioner successfully maintained that the interest claimed as a deduction, and taken into account in calculating the losses sustained by the receivership company, was cancelled as a consequence of the liquidation of that company. In the course of the judgment, Thomas J made the following observations in relation to statutory interpretation –

> It is the Court's task to promote Parliament's intent, not to frustrate it. In *IR Commrs v McGuckian* [1997]

3 All ER 817, Lord Steyn (at p 824), delivering the main judgment, confirmed that the modern purposive approach to statutory construction applies to tax legislation no less than other legislation. The literal interpretation of tax statutes has given way to the purposive approach which requires the Court to consider the context and scheme of the Act as a whole and to have regard to the purpose of the legislative provision. See also *WT Ramsay Ltd v IR Commrs* [1982] AC 300, per Lord Wilberforce at p 323.

The purposive approach to statutory interpretation is well developed in New Zealand. Elaborating on what is meant by the purposive approach warrants a whole paper in itself. It is not entirely accurate to say that the literal interpretation has given way to the purposive approach – the starting premise in interpreting a statute lies with the words actually used. The purposive approach is usually adopted if there is a good reason to do so and some commentators view the approach as an exception to the literal approach. In appropriate cases, this approach can be used as a tool against tax avoidance, although it is an approach that can equally assist taxpayers (New Zealand Courts have on a number of occasions confirmed that a GAP is to be given a purposive construction). It does not follow from the above passage that Thomas J has embraced the fiscal nullity principle. However, given that *Ramsay* and *McGuckian* were also referred to by His Honour in *Peters v Davison (No 3)* (1998) 18 NZTC 14,027, albeit as support for the purposive approach, the intended extent of their application is not entirely clear. It has to be remembered that a pure fiscal nullity approach strikes down transactions that have no business or commercial purpose. This approach has never been accepted in New Zealand as we have a GAP, taxation by economic equivalence is impermissible and form over substance generally prevails. It is possible to relevantly explain fiscal nullity in a New Zealand context as a form of construction approach or a by-product of statutory interpretation, but no more. See also the comments below in relation to *BNZ Investments*.

The purposive approach to tax legislation is supported by the following:

- section AA 3 of the Income Tax Act 1994 which provides that the meaning of a provision of the Act is found by reading the words in context and, particularly, in light of the purpose provisions, the core provisions and the way in which the Act is organised;
- section 5 of the Interpretation Act 1999 – which provides that the meaning of an enactment must be ascertained from its text and in the light of its purpose;
- recent Court of Appeal cases have highlighted the scheme and purpose approach to interpretation in revenue cases – see *CIR v Alcan NZ Ltd* [1994] 3 NZLR 439 and *Tasman Forestry Ltd v CIR* [1999] 3 NZLR 129 (where at para [25] Gault J observed: "It is, of course, entirely appropriate to seek to identify the scheme and purpose of statutory provisions as a guide to interpretation".) Interestingly, these cases are not referred to in the judgments of Thomas J.

BNZ Investments Ltd

In *BNZ Investments Ltd v CIR* (2000) 19 NZTC 15,732, the High Court ruled in favour of BNZ Investments Ltd ("BNZI") on the issue of whether its limited participation in a series of complex transactions constituted a tax avoidance arrangement under s 99 of the Income Tax Act 1976. The judgment is very long and will no doubt be the subject of much analysis and commentary. In very abbreviated terms, BNZI made a series of redeemable preference share investments and the trans-actions resulted in the funds being deposited with prime overseas banks, with interest earned ultimately repatriated to BNZI as exempt dividends. One of the features was the ability to convert a taxable income stream from offshore into a non-taxable income stream in New Zealand through use of specific rules.

The major principles stemming from the judgment are:

- McGechan J endorsed the purposive approach to statutory interpretation (literal interpretation is not the approach in cases of avoidance and sham and, in addition, s 5 of the Interpretation Act 1999 is to be followed);
- the overall concept of an arrangement under a GAP entails "conscious involvement" by the parties to an end ie mere suspicion or knowledge that there may be avoidance by other parties elsewhere in the transaction is not sufficient;
- it would be superficial to say that a GAP is intended to suppress tax avoidance and should be interpreted in whatever way it best does so, without limit. Parliament's concerns lie with organised attacks on the tax base, as contrasted with a mere random event (in here I would add genuine transactions) the incidence of which can be allowed for and tolerated;
- the *Ramsay* fiscal nullity doctrine does not assist the question of whether there is an "arrangement" and the doctrine is unhelpful in New Zealand. The only useful application of the doctrine may be in ascertaining the "purpose" of an arrangement but not its scope. There are clear indications in the judgment that fiscal nullity is difficult and not useful to apply in New Zealand;
- tax avoidance purpose will be evidenced by extraordinarily and unnecessarily complicated steps/transactions.

In the discussion of *Miller*, McGechan J observed that reconstruction under a GAP can only take place if the taxpayer has obtained a "tax advantage". For a tax advantage to occur, there must have been an alteration in tax which otherwise would have been imposed. This requires a change in the base tax and the concept of "tax advantage" does not mean "economic advantage". One of the purposes of a GAP was seen as the preservation of the tax base. Therefore, where tax advantages are increased through avoidance over a base level which would have existed in any event, it is that increment above base level which is to be counteracted, not the legitimate base level itself.

CONCLUDING REMARKS

Recent capital/revenue cases have largely turned on their facts. With perhaps the exception of *Birkdale* (which I consider is a difficult case), most would agree that the Courts have reached correct decisions. The judgment of Blanchard J in *Miller* is fascinating and, although at first blush seems to mandate a broad approach (in favour of the Commissioner), it is for the most part possible to reconcile the judgment with existing principles.

Increasingly, New Zealand Courts are adopting, in appropriate cases, a purposive approach to the interpretation of tax statutes and this is entirely sound as a matter of law and principle. Finally, trends in recent New Zealand tax cases, in my view, indicate that Courts are embracing income tax as a body of principle in a way that will ultimately preserve the integrity of the tax system. *Wattie* is a prime example of this. ❑

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