

Legal update on Banking and Commercial Law.

IN THIS ISSUE

BANKING

- [Australian PPSA implementation update](#)
- [Case review - demands continue upon dispute](#)
- [Case review - Scope of Guarantee - Boilerplate provision useful](#)
- [CCCFA banning order for lender following "outrageous" conduct](#)
- [Australian Bank Fees and the law in relation to penalties generally – John Andrews v Australian and New Zealand Banking Group Limited \[2011\] FCA 388](#)

COMMERCIAL

- [Amalgamation loophole to be closed](#)
- [Warning for "patsy" directors](#)
- [New Zealand PPP environment improves](#)

BANKING

AUSTRALIAN PPSA IMPLEMENTATION UPDATE

Those with interests in personal property in Australia should note that the operational commencement date of the Australian Personal Property Securities Act 2009 (PPSA) had been further deferred until sometime in 2012.

The Personal Property Securities (Registration Commencement) Bill 2011, was passed on 24 November 2011. The Bill amends the definitions of "migration time" and "registration commencement" time so that the Attorney-General may determine a time other than the automatic times in the PPSA. This will provide additional flexibility to the commencement date, which could be utilised if any unforeseeable issues arise in the final weeks before the planned commencement time of 30 January 2012. A determination by the Attorney-General setting the revised commencement date is expected in early 2012.

The key factors noted in relation to the amendment are as follows:

- Data migration and preparatory registration are key components of the Australian personal property securities reform. The system must be stable to ensure a seamless transition to the new personal property securities regime

- The amendment will ensure that the operative provisions will not automatically commence before the single national online register is available for public use and industry and users are ready for the new national scheme.

For those that wish to monitor and gain further information on the above developments (for instance, so as to ensure continuous perfection of security), please click [here](#).

[Back to top>>](#)

CASE REVIEW - DEMANDS CONTINUE UPON DISPUTE

A recent Court of Appeal case, *21st Century Investments Ltd v ANZ National Bank Ltd* [2011] NZCA 548, confirmed that demands will be effective even when some components of the demand are under dispute. Creditors may still exercise remedies relying upon the demand, such as acceleration, but they must relate to amounts that remain undisputed and unpaid after the relevant notice period.

21st and ANZ were party to a term loan agreement pursuant to which monthly payments of interest were required. The agreement also provided as a general rule that all payments were to be made "on demand". ANZ issued two demands for unpaid interest instalments and various other arrears. 21st disputed some, but not all, of the amounts. When the notice period expired, ANZ remained substantially unpaid in respect of the amounts demanded and sought to accelerate the entire loan.

On appeal, the Court upheld the earlier Associate Judge's refusal to set aside the demand in full, as no substantial injustice would result if it were not set aside, and a miscalculation of some amounts did not invalidate the entire notice.

The Court also accepted that ANZ's power to accelerate was not extinguished by the partial dispute of the amounts in the demand. A default of "any" undisputed amount in the demand entitled ANZ to accelerate the loan. The Court held that the monetary value of the default was irrelevant; and the Court was unwilling to imply a restriction upon the exercise of acceleration that the parties did not agree upon.

The Court also considered the amount of time required to be given to debtors to remedy a payment demand. After surveying relevant authority the Court confirmed that because most debtors are not expected to hold large cash reserves, creditors should allow debtors "reasonable" time to convert their presently available resources into cash (but need not be allowed time to seek out new resources for payment). What constitutes reasonable time will depend on the circumstances in each case. In this case 21st was given two days to make payment in remedy of the demand and the Court held this was reasonable time in the circumstances.

[Back to top>>](#)

CASE REVIEW - SCOPE OF GUARANTEE - BOILERPLATE PROVISION USEFUL

The additional boilerplate of the type that is usually added to a guarantee recently worked to enable RD1 Ltd to recover under its guarantee when otherwise it may not have been able to.

In the case of *RD1 Ltd v McKinnon* HC Auckland CIV-2011-404-003499 [4 November 2011], RD1 provided products to the debtor on credit, and Mr McKinnon guaranteed the debtor's payment obligations to RD1. The contract between RD1 and the debtor initially specified a credit limit of \$2,000, but RD1 continued to supply products on credit in excess of the limit, totalling over \$20,000. When the debtor defaulted on payment, RD1 sought payment from Mr McKinnon under the guarantee, but the District Court held that RD1 could recover from the guarantor only up to the credit limit of \$2,000.

The High Court overturned this District Court decision, holding that the \$2,000 credit limit was not a term of the guarantee. The guarantee expressly provided that the terms on which credit is given may be varied, and that the guarantee will continue even though those terms are changed. The Court therefore held that the guarantee allowed RD1 to recover from the guarantor credit in excess of the limit, and ordered Mr McKinnon to pay the full amount owing by the debtor to RD1.

This case is a useful reminder that express terms of a guarantee can negate the application of the principle that a substantial variation of the underlying credit contract between the debtor and creditor without the consent of the guarantor will discharge the guarantor from liability. These types of provisions are usually included in longer forms of guarantee precedent but can be cut by drafters seeking a shorter guarantee. Eliminating them to shorten a guarantee is not without risk.

[Back to top>>](#)

CCCFA BANNING ORDER FOR LENDER FOLLOWING "OUTRAGEOUS" CONDUCT

Convicted fraudster and bankrupt Trevor Allan Ludlow has been issued with a banning order under section 108 of the Credit Contracts and Consumer Finance Act 2003 (CCCFA). The order, which is the first of its kind issued under the CCCFA, prevents him from setting up, operating or working in the consumer finance industry. The banning order together with fines and reparation were ordered following a case against Takarunga Management Limited, trading as Mortgage Rescue, and its director and sole decision-maker Trevor Ludlow under the CCCFA and the Fair Trading Act 1986.

Judge Hinton observed that Ludlow's response to borrowers cancelling their contracts or disagreeing with him was "clearly unlawful and in the circumstances, outrageous". Ludlow "lacked the skills to be in the industry" and did not "display the integrity and fair dealing that is appropriate in this type of dealing".

The Commerce Commission prosecuted Mortgage Rescue in relation to two consumer credit contracts. In the first case, Mortgage Rescue charged a cancellation fee of \$5,000 and a legal fee of \$1,500 (when it had only paid \$675 for legal services) when the borrowers cancelled the contract the day after they entered into it. Both the company and Ludlow were convicted of charging an unreasonable cancellation fee and the company was convicted of not passing on the "actual" legal fee as required under the CCCFA.

In the second case, Mortgage Rescue tried to recover more than the loan amount for renovation work it had carried out on the property. Mortgage Rescue issued a default notice and sold the property. The Court found that Mortgage Rescue had misrepresented the amount that it could recover, as it had not disclosed any variation to the loan amount. Mortgage Rescue also had no right to charge a services fee as it had not arranged a refinance, and it had served the default notice before it was legally entitled to make a demand for payment. Mortgage Rescue was convicted of all three charges and Ludlow on two of the three.

While there are frequent demands for even greater levels of consumer credit law protection, these have the potential to add cost and red-tape for all participants in the industry, not just the ratbags. It is pleasing to see greater use being made of the existing powers to target the worst offenders.

[Back to top>>](#)

AUSTRALIAN BANK FEES AND THE LAW IN RELATION TO PENALTIES GENERALLY – JOHN ANDREWS V AUSTRALIAN AND NEW ZEALAND BANKING GROUP LIMITED [2011] FCA 388

The Federal Court of Australia (Melbourne) released its preliminary decision on 5 December 2011 in a case concerning the legal status of particular bank fees. The case is also of interest as a comprehensive analysis on the law relating to penalties more generally.

In *Andrews v Australian and New Zealand Banking Group Limited*, Australia's largest class action, three ANZ customers sought to argue that certain exception fees they had been charged by the bank constituted penalties and were hence void or unenforceable (in a bid to recover as much as A\$5 billion that Australian account holders paid in fees in the past six years).

The law in relation to penalties in both Australia and New Zealand is that a contractual provision which requires the payment of a specified sum upon breach of the contract may not be enforceable if such specified sum is not a genuine pre-estimate of the loss flowing from the breach of the relevant obligation.

In this preliminary decision, however, the quantum of the fees was not at issue (and ANZ accepted that the exception fees did not constitute a genuine pre-estimate of damage). Gordon J confined her judgment to the question of whether each of the fees was of a type within the ambit of the rule against penalties.

After undertaking a lengthy examination of the law of penalties, Gordon J emphasized that the rule against penalties constitutes an exception to the principle of freedom of contract. She thus rejected attempts to expand the rule to cover contractual provisions requiring payment of a sum upon the happening of an event which does not constitute a breach of contract.

Her Honour then turned to consider the particular types of fees at issue in the case:

- Honour fees, charged when a customer overdraws, or exceeds the maximum credit limit of, his or her account without prior approval from the bank (i.e. clearing a cheque even when the account balance was insufficient to cover the amount paid)
- Dishonour fees, charged when any payment on an account is dishonoured due to insufficient cleared funds (i.e. bounced cheques)
- Overlimit fees, charged at statement date if the balance of a credit card account exceeds the limit at any time during the statement period
- Non-payment fees, charged when the customer has authorised a payment that is not made due to a lack of cleared funds in his or her account
- Late payment fees, charged when the customer has failed to pay the minimum amount due on his or her credit card by the due date.

Gordon J concluded that the first four types of fees listed did not come within the ambit of the rule against penalties, because they do not become payable upon a breach of contract by the customer. Rather, they were fees charged by the bank for exercising a discretion (in either accepting or not accepting the customer's request to overdraw their account or exceed their limit) which the customer has asked it to exercise by requesting the bank to make the payment. By contrast, the late payment fees were capable of being characterised as penalties because they were triggered by a breach of a contractual obligation - being the customer's failure to pay a minimum amount by a particular date.

A trial next year will determine whether the late payment fees at issue are, as a matter of fact, sufficiently excessive and unconscionable to constitute penalties having regard to the burden they imposed on customers compared with the loss incurred by the bank due to the breach.

In New Zealand, as in Australia, it is accepted that the rule against penalties applies only where there has been a breach of a contractual obligation. Gordon J's conclusions on the legal status of particular fees may prove persuasive to New Zealand courts, although in the case of consumer credit contracts, the Credit Contracts and Consumer Finance Act 2003 provides an additional overlay as it requires that a consumer credit contract must not provide for a credit fee or a default fee that is "unreasonable".

[Back to top>>](#)

AMALGAMATION LOOPHOLE TO BE CLOSED

Much to the frustration of the Takeovers Panel, since the Takeovers Code was introduced "long form" amalgamations under Part 13 of the Companies Act 1993 (Act) have provided Code companies with an alternative mechanism to effect a merger - a mechanism that is often more efficient and flexible than a Code offer. However, a recent Bill supported by the Panel makes inroads into closing this perceived loophole.

The Companies and Limited Partnerships Amendment Bill (Bill) was introduced to Parliament on 13 October 2011. Amongst other changes to the Act and the Limited Partnerships Act 2008 (which were summarised [here](#)), the Bill removes the ability for a code company to effect an amalgamation under Part 13 of the Act. The proposal is a significant step in increasing the oversight of the Takeovers Panel on mergers of larger or publicly listed companies.

The amendments would leave Code companies with the option of using a court approved scheme of arrangement to implement a merger under section 236(1) of the Act (thereby avoiding a Code offer). The Bill bolsters the provisions relating to schemes of arrangement by requiring the Panel to be notified as well as the following pre-requisites:

- Voting thresholds: The scheme must be approved by an ordinary resolution of shareholders, as well as a special resolution (75% majority) of shareholders in each interest class
- Shareholders not disadvantaged: The Code company must either:
 - prove that avoiding the Takeovers Code will not adversely affect the company's shareholders; or
 - obtain a "no objection" statement from the Takeovers Panel (the process of which is yet to be determined).

Whether the new scheme of arrangement process in the Bill will be widely used will depend to a large extent on the Panel's willingness to consider alternatives to the Code procedures, and the Courts' ability to deal with applications for schemes of arrangements quickly and decisively.

The Bill is likely to go through a first reading and be sent to the Commerce Select Committee early in the new year, at which point we expect interested parties will be given an opportunity to make submissions. [Back to top>>](#)

WARNING FOR "PATSY" DIRECTORS

A recent High Court case serves as a warning to directors of companies who act on the instructions of controlling shareholders (sometimes known as "nominee" directors).

The case (*Blanchett v Keshvara*, High Court, Auckland, 13 September 2011 (CIV2010-404-001282)) was brought by the liquidators of A.P.G. Holdings Limited against Mr Keshvara who was a former director of the company.

The company was part of the failed Capital Events Group which was controlled by Terry Wilson and Andrew Tauber and had been involved in providing hospitality services for sporting and cultural events. According to the liquidators, in 2004 Mr Keshvara had allowed the company to pay more than \$1.4 million to certain individuals and companies associated with Mr Keshvara, Mr Wilson and/or Mr Tauber including in one case Mr Wilson's daughter.

The payments were described as unsecured loans. However the liquidators could find little or no documentation in relation to the payments and no evidence was adduced by Mr Keshvara. There appeared to have been no inquiries into the ability of the borrowers to repay the loans or any arrangements made for interest or repayment. Needless to say the loans were not repaid.

In essence the liquidators' case was that when the payments were made the company was insolvent, that the payments were not in the company's best interests and that there was no proper purpose for them.

The Court observed that Mr Keshvara appeared to be a nominee or "patsy" director who was accustomed to act on the direction of others (probably Messrs Wilson and/or Tauber). However the Court gave short shrift to the suggestion that as such Mr Keshvara should be subject to a lesser standard than an executive director.

The issue was simply whether acts of Mr Keshvara breached the duties he owed to the company as a director, and if so then he was liable to the company for any losses as a consequence of that breach. The relevant duties Mr Keshvara owed to the company included common law fiduciary duties and statutory duties under sections 131 and 133 of the Companies Act 1993, in particular duties to act in good faith and in what he believed to be in the best interests of the company and to exercise his powers for a proper purpose.

The result was that Mr Keshvara was ordered to pay the company the amount of the loans advanced to the various related parties, these exceeded \$1.4 million.

The case illustrates the personal risks associated with the role of director and the importance of understanding that the duties are owed primarily to the company rather than those whom the director might receive instructions from.

[Back to top>>](#)

NEW ZEALAND PPP ENVIRONMENT IMPROVES

The Office of the Auditor-General has published a Discussion Paper on "*Managing the implications of public private partnerships*" (PPPs). The Discussion Paper aims to inform readers about the opportunities and challenges of PPPs to the public sector and to encourage informed debate on the topic.

In the paper the Auditor-General, with the assistance of a "maturity" analysis prepared by Deloitte, takes a look at perceived benchmark criteria for effective PPPs and identifies where New Zealand sits against those benchmarks. Overall New Zealand is considered as having moved from a "developing" PPP market in 2006 to an "active" PPP market in 2011 but is still short of being a well-functioning and "mature" PPP market (such as Australia or the United Kingdom).

Areas identified where advances have been made include:

- Improved understanding of the commercial principles of PPPs and more experience of transactions by public and private sector
- Improved standards of public sector governance and procurement, with effective evaluation and award criteria
- New Zealand having an established common law tradition, based on respect for contracts, transparency, and good standards of governance. (To get to the next stage a standard contract is seen as being essential for delivering effective PPPs.)

Some of the areas identified where improvements are required before New Zealand has a well-functioning (or mature) PPP market include:

- Gaining further experience in identifying and allocating risk (i.e. developing standardised sector specific risk allocation processes which can provide a starting point for negotiations)
- Building domestic and private sector skills (especially in smaller organisations which currently lack the resources to access PPP knowledge or experience)
- Improved sophistication (and financial instruments) in the domestic capital markets, which currently suffer poor liquidity in the long-term debt market and few specialised domestic equity sponsors.

The Discussion Paper can be found [here](#).

[Back to top>>](#)

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