BUDDLE FINDLAY

Legal update on litigation and dispute resolution - May 2015

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Apparently not: principal cloaks agent in apparent authority, but saved by counter offer

In *Pascoe Property Limited v Attorney General* [2014] NZCA 616, it was nearly the case that a commercial agent bound the Ministry of Economic Development (Ministry) to a renewal of a lease, despite that commercial agent not having actual authority from the Ministry to execute legally binding documents.

A senior employee of the Ministry had told the landlord, Pascoe, that the commercial agent would be responsible for negotiating the renewal of the lease. The commercial agent had frequently spoken on behalf of the Ministry, and had signalled the fact of agreement to Pascoe. The Ministry was copied in on all of the commercial agent's correspondence and took no steps to clarify, as a matter of internal policy, that the commercial agent had no authority to execute legally binding documents. The Court of Appeal concluded that the Ministry had cloaked the commercial agent with apparent authority and as such he was capable of binding the Ministry to the renewal.

The saving grace for the Ministry was that after receiving a letter containing the terms on which the renewal might proceed, the landlord had made handwritten alterations before signing and returning it. That amounted to a counter offer, which remaining unaccepted prevented the Ministry from being bound to any renewal.

The near miss for the Ministry is a good example of the need for the authority of agents in contractual negotiations to be clearly communicated and recorded by their principals. The decision also demonstrates the need for principals to take active steps to clarify miscommunication of authority by agents. The failure to do so risks a party being bound to a contract to which they did not formally consent.

See Court decision here.

A dangerous undertaking: accountant liable for misleading statement

The High Court decision in *Swindle & Others v Withers & Anor* [2015] NZHC 888 serves as a reminder to professionals such as accountants that they should not give undertakings unless they have confirmed that those undertakings are accurate and that they are able to comply with them. A failure to do so may result in liability for misleading and deceptive conduct under the Fair Trading Act 1986.

The case arose after the plaintiff lenders agreed to advance funds to various companies involved in winemaking. The lenders claimed that they made the advances in reliance upon an undertaking given by the borrowers' accountant, Mr Withers, that he was a mandatory joint signatory to the borrowers' "costs account" and that the costs account would only be used to meet certain specified production costs.

It was not in dispute, contrary to the statement in the undertaking, that Mr Withers was not a signatory to the relevant account. However, he raised a number of defences, including that the undertaking was not misleading because he believed that he was committing to be a signatory to the account, that he relied upon the borrowers to make the necessary arrangements and that if he were presented with a cheque to sign, he would ensure that it was to pay a production cost. The Court held that this was not the impression conveyed by the undertaking, which was a statement of fact. It also observed that Mr Withers had acknowledged in evidence that he knew that his undertakings would be relied on by the lenders and that he had sent an email to the borrower after giving the undertaking querying whether the account was being operated in accordance with the undertaking, but that he had failed to raise the matter again when he did not receive a response.

The Court found that Mr Withers' misleading conduct caused the loss claimed by the lenders, but held that the lenders had also contributed to their own loss, including by failing to take quick and appropriate action after they should have been put on notice of the borrowers' financial position. As a result, it ordered that Mr Withers should bear only half of the plaintiffs' total loss.

See Court decision here.

Listen to the expert: court unable to intervene in an expert determination process

It is not uncommon for parties involved in disputes of a technical nature to agree that such disputes are to be resolved by way of "expert determination" rather than by litigation in the courts or by arbitration. *Marquis Property Developments Limited v Lorenzen & Ors* [2015] NZHC 694 illustrates that where a clear agreement that an expert is to be sole decision-maker has been reached, the parties may not then ask the Court to resolve the dispute.

The case arose after the parties referred three disputed claims to expert determination. The parties asked the expert to review certain aspects of his decision, including because it did not deal with one of the claims. The expert refused to do so, on the grounds that he was *functus officio* (ie he had performed his role), so the plaintiff asked the Court to determine its claims.

The Court refused to do so, noting that the agreement between the parties as to expert determination explicitly stated that once the expert's decision was issued, no further legal action would be commenced or continued except in relation to the enforcement of that decision. It also disagreed that the expert was *functus officio*. He had not determined all aspects of the claims and it was not open to him to determine his status in this way – the issue of that status being a matter of fact and law. The Court observed that, just as a Court may recall its judgment where by oversight it fails to deal with an issue raised by a party, so the expert could recall his original determination in order to deal with the issue he originally failed to rule on.

The decision illustrates the importance of choosing the right expert in an expert determination and ensuring, if it is intended that there is to be a right of appeal from his or her decision, that right is expressly documented in the relevant agreement.

See Court decision here.

Court of Appeal rules on the unreasonableness of credit and default fees under the CCCFA

Sportzone Motorcycles Ltd (Sportzone) sold motorcycles and, in conjunction with Motor Trade Finances Ltd (MTF), provided credit to consumers to purchase those motorcycles. The credit agreements were subject to the Credit Contracts and Consumer Finance Act 2003 (CCCFA), which provides that credit providers are allowed to charge reasonable fees that are connected to the provision of the credit in relation to a particular consumer.

The arrangement between Sportzone and MTF was that Sportzone borrowed from MTF in order to provide finance to its customers and assigned its interest in the customers' loans to MTF. Both Sportzone and MTF charged the customers establishment and maintenance fees, and MTF also charged prepossession and repossession fees in the event of default. The fees charged by MTF were paid by Sportzone and passed on to the customers. The Commerce Commission issued proceedings against Sportzone and MTF, alleging that their establishment, credit and default fees were unreasonable for the purposes of the CCCFA, as both parties had charged back a number of unrelated indirect and fixed costs to consumers through those fees.

In *Sportzone Motorcycles Limited (In Liq) v Commerce Commission* [2015] NZCA 78, the Court of Appeal upheld the decision of the High Court that the fees were not reasonable, as they were not connected and did not have close relevance to costs or losses incurred in the establishment and management of the customers' accounts. In particular, the fees sought to recover fixed cost items such as premises rent, telephone and electricity costs, insurance, rates, system development etc and could not be said to be incurred in sufficient connection with the particular transaction.

The Court of Appeal held that the Commerce Commission could claim back (on behalf of the consumers involved) the amount by which the fees had exceeded what the creditors were lawfully entitled to charge. The Court of Appeal's judgment also contains guidance on the proper accounting approach flowing from its interpretation of the statutory provisions. In particular, creditors can claim back through fees their variable costs (costs that change depending on the number of people obtaining loans) and some closely connected fixed costs.

See Court decision here.

Declaration of future intention does not create express trust

A v C [2014] NZHC 3009, provides useful guidance of what is required in order for an express trust to be created – confirming that promises as to what might happen in the future will not meet the threshold.

A's litigation guardian sought to uphold a caveat lodged on her behalf against property owned by her father, on the grounds that he had placed the property on trust for A as part of a settlement when A's parents separated in 2005. The father denied that he

held the property on trust for A.

The Court found it was not reasonably arguable that the father had intended to create an express trust in A's favour. An express trust requires certainty of intention, subject matter and object. The intention must be to create a present trust. In this case, the promise to transfer the property to A (or if A was no longer living, whichever other class of beneficiary was living at the time) upon termination of the mother's life interest in the property, at an unknown time in the future, was insufficient.

Further, at the time the promise was made, due to the mother's life interest, the father only had an interest in part of the property. This confirmed that the promise was inconsistent with the alleged intention to relinquish immediately the beneficial interest in the whole property. At most, A had a right to enforce her father's promise to create a trust at a future time (ie when her mother's life interest terminated). However, that was not the interest the caveat claimed to protect. Accordingly, the application to prevent the caveat from lapsing was dismissed.

Constructive notice of fraud for banks

In *Credit Agricole Corporation and Investment Bank v Papadimitriou* [2015] UKPC 13, the Privy Council restated and refined the test for determining whether a party (Party A) has constructive notice of fraud so as to enable a third party (Party B) to assert a proprietary claim against Party A in respect of assets which Party B has been able to trace into the hands of Party A.

In this case, the respondent (being Party B) brought a claim against the Bank (being Party A), alleging a proprietary right to the proceeds of sale deposited with the Bank in respect of an antique collection, which had been owned by the respondent's deceased father, but was fraudulently sold by a family friend. A large portion of the sale proceeds were deposited with the Bank and involved in a complex web of transactions involving several foreign entities.

The issue for the Privy Council was whether the Bank was on constructive notice of the impropriety or was a bona fide purchaser without notice, and whether the Court of Appeal, in overturning the decision of the trial judge and allowing the respondent's claim, had applied the correct legal test.

The Privy Council considered in what circumstances and to what extent the Bank should have made inquiries or sought advice. The Privy Council held that the Bank's knowledge of facts indicating the mere possibility of a third party having a proprietary right would not be enough to put the Bank on inquiry. Rather, the test must be that the Bank must make inquiries if there is a serious possibility of a third party having such a right. The test was stated in the following terms: "*…if the facts known to the Bank would give a reasonable banker in the position of a particular banker serious cause to question the propriety of the transaction*."

The Privy Council confirmed the Court of Appeal's finding that, on the whole, the Bank had been on constructive notice of impropriety as on the facts actually known to the Bank, there was no apparent explanation of the interposition of the foreign entities unless it was to conceal the origin of the funds.

See Court decision here.

A blow for fraudulent directors as UK Supreme Court rules on the application of illegality defence

In *Jetivia SA and another v Bilta (UK) Ltd and others* [2015] UKSC 23, the UK Supreme Court considered rules of attribution and the application of *ex turpi causa non oritur actio* (the illegality defence, which bars a party pursuing a legal remedy if it arises in connection with the party's illegal act) in the context of VAT fraud perpetrated by the directors of Bilta and assisted by Jetivia and its director. The question for the Court was: if the directors of a company involve the company in a fraudulent transaction, is the company barred by virtue of the illegality defence from suing those directors and their accessories for losses caused by their breach of fiduciary duty?

Jetivia relied on the case of *Stone & Rolls Ltd v Moore Stephens* [2009] UKHL 39 to argue that the company was barred from bringing such a claim. In *Stone & Rolls* the auditors of a company whose sole director had used the company to perpetrate fraud were successful in relying upon the illegality defence to bar a claim by the liquidators against the auditors for negligence in failing to detect the fraud. Bilta's liquidators sought to distinguish *Stone & Roll*s (on the basis that the fraud in that case was against a third party and not the company itself) and argued that company directors who have been fraudulent should not be able to rely on their own fraud in order to defend themselves against a claim by the company.

The Supreme Court unanimously dismissed Jetivia's appeal, holding that the illegality defence did not bar the company's claims against the directors and their accessories. The Court considered that the finding in *Stones & Rolls* that dishonest directors, and those assisting them, cannot rely on their own wrongdoing to escape liability, was distinguishable in this case on the basis that the acts of such directors cannot be attributed to the company. The Supreme Court stated that the law around the illegality defence would need to be considered and clarified at some point, but that this was not the appropriate case in which to do so. However, in the interim the Supreme Court was eager to limit the application of *Stone & Rolls* to its specific fact scenario, namely cases where

a claim was being brought by a company against a third party, rather than against fraudulent directors themselves.

See Court decision here.

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