Stiassny v North Shore City Council

Court of Appeal Wellington CA 713/07; [2008] NZCA 522
21 October; 2 December 2008
William Young P, Glazebrook and O'Regan JJ

Contract – Agency – Whether relationship of principal and agent or debtor and creditor.

Commercial law – Personal property securities – Whether beneficial interest in trust fund amounted to security interest – Observation – Personal Property Securities Act 1999, s 17.

North Shore City Council operated a weekly refuse collection and disposal service. To recover the cost of providing this service, the Council required users to place refuse in branded plastic bags for collection. The Council entered into a contract with Chequer Packaging Ltd (CPL) whereby CPL would supply, merchandise and distribute the bags. CPL would sell the bags to retailers at a set price. The price was made up of the fees charged by the Council for collection, plus CPL's merchandising and distribution fee. The Council would then invoice CPL for the collection fees.

CPL went into receivership and the receivers applied to the High Court for directions as to whether the Council had a proprietary interest in the fees portion of the sale price. The High Court held that the relationship of the Council and CPL was not one of principal and agent, with the result that CPL was not holding the collection fees on the Council's behalf. The High Court observed that even if the Council had had a proprietary interest in the collection fees, that interest would have constituted a security interest for the purposes of the Personal Property Securities Act 1999 and would have ranked after the security of the appointer. The Council appealed.

Held: The critical issue in determining whether the arrangement was of an agency-trust or debtor-creditor nature was whether the supplier was required to keep the funds in a separate account. Whether it was right to start with a presumption against an agency-trust arrangement was open to question, but the usual incidents of a commercial arrangement whereby there were a series of running transactions indicated that there had been no requirement to keep the funds separate (see paras [20], [22]).

Result: Appeal dismissed.

Observation: The proprietary interest of a beneficiary under a trust alone will not necessarily amount to a security interest for the purposes of the Personal Property Securities Act as it does not secure any obligation independent of those arising from the trust (see para [29]).

Cases mentioned in judgment

Henry v Hammond [1913] 2 KB 515.

Paragon Finance plc v D B Thakerar & Co (a firm) [1999] 1 All ER 400 (CA).

Walker v Corboy (1990) 19 NSWLR 382 (NSW:CA).

Westpac Banking Corporation v Savin [1985] 2 NZLR 41 (CA).

Appeal

This was an appeal by North Shore City Council from the decision of Harrison J (reported at [2008] 1 NZLR 825) in which Michael Peter Stiassny and Brendon James Gibson as receivers of Chequer Packaging Ltd (in receivership) (CPL) had successfully applied for directions that the Council did not have a proprietary interest in part of the proceeds of sale of official refuse bags sold by CPL to retailers.

C R Carruthers QC and *F C Monteiro* for the Council.

R B Stewart QC and *L A O'Gorman* for the receivers.

Cur adv vult

The judgment of the Court was delivered by

WILLIAM YOUNG P. [1] North Shore City Council (NSCC) provides a weekly curbside refuse collection and disposal service for households and businesses within its district. From July 2006, refuse had to be in branded bags in order to be collected. These bags were available for purchase from retailers, which is where Chequer Packaging Ltd (CPL) came into the picture. It both supplied the bags and merchandised and distributed them to retailers.

[2] The retailers paid CPL for the bags at prices which were agreed between NSCC and CPL. Later, CPL paid to NSCC the amounts which the retailers had agreed to pay for the bags less an agreed margin for the cost of supplying, mechandising and distributing the bags. With this revenue NSCC funded its refuse collection and disposal service.

[3] On 23 January 2007 CPL was placed in receivership. The current litigation concerns the entitlement (or otherwise) of NSCC to payments made by retailers to CPL after it went into receivership. NSCC claims, and the receivers of CPL deny, that under the relevant contractual arrangements between CPL and NSCC those payments belong in equity to NSCC. In the alternative, the receivers claim that if the relevant contractual arrangements have the effect contended for by NSCC, they create a security interest which, under the Personal Property Securities Act 1999 (the PPSA), ranks after the security interest of their appointor.

[4] In the High Court, Harrison J found in favour of the receivers on both grounds ([2008] 1 NZLR 825). NSCC now appeals.

[5] We will address the appeal by reference to the following headings:

(a) the contractual arrangements;

(b) whether the payments made by retailers belong in equity to NSCC; and

(c) the PPSA issue.

The contractual arrangements

The substance of what NSCC wished to achieve

[6] Before the relevant contractual arrangements were entered into, NSCC called for tenders in relation to the supply, merchandising and distribution of the bags. The tender documentation stipulated (albeit on an indicative basis) the prices at which the bags would be sold to the retailers, and also the supplier's merchandising and distribution fee (fixed at 2 cents per bag). The purpose of the tender process was thus to obtain a competitive price for the supply of the bags. The tender process resulted in CPL being the preferred tenderer.

[7] The indicative price identified in the tender process and later charged to the retailers was $1.135 per bag. Of this, 2 cents represented the merchandising and distribution fee for CPL, which we have just mentioned. CPL was also entitled to be paid for the supply of the bags, and the figure for this which came out of the tender process was 12.5 cents per bag. So of the price payable by the retailers for each bag, 14.5 cents was to the credit of CPL and the balance (99 cents) was to be paid to NSCC.

[8] Primarily NSCC sought to obtain a revenue stream which would meet the costs of providing its refuse collection and disposal service. But it had other, ancillary, objectives as well. In particular it wanted the system to operate on the basis that CPL dealt directly with the retailers (with CPL responsible for merchandising and distribution and taking all associated credit risks), and did not wish itself to maintain an inventory of bags.

Possible legal mechanisms

[9] Broadly speaking there were two options by which the economic and other results sought by NSCC could be achieved:

(a) First, there could have been what we will call an "agency-trust arrangement". Under such an arrangement, NSCC (through the agency of CPL) would sell the bags to the retailers and, as vendor of the bags, be entitled to the proceeds of sale. This would require either NSCC to pay CPL 14.5 cents per bag or CPL being authorised to deduct this from what it held on behalf of NSCC. Leaving aside PPSA complications, such an arrangement would have given NSCC control and security over the cash flow from the retailers and thus limited its credit exposure to CPL.

(b) Secondly, there could be what we will call "a debtor-creditor arrangement". Under such an arrangement, there would simply be a series of running accounts between (i) CPL and retailers; and (ii) CPL and NSCC.

[10] With the benefit of hindsight, it would be easy to conclude that NSCC should have made unequivocal provision for an agency-trust arrangement. But what might be thought to be the usual corollaries of an agency-trust arrangement did not fit in well with NSCC's ancillary objectives. We say this because if NSCC had insisted on an agency-trust arrangement, CPL would be likely to have required that NSCC: (i) take the credit risk on the retailers; and (ii) obtain (and pay for) an inventory of bags from which supplies to retailers could be made. As well, CPL might have cavilled at the administrative costs and inconvenience of operating a separate bank account in which to hold payments from retailers. So while a debtor-creditor arrangement would not

offer the same security as an agency-trust arrangement, it would be more congruent with NSCC's ancillary objectives (referred to at para [8] above) and probably cheaper to operate.

The contractual documents

[11] The proposed contractual documentation which formed part of the tender process did not identify with clarity which of the two arrangements was proposed. The waters were further muddied when CPL and NSCC agreed on invoicing arrangements that differed from those contemplated in the original tender documentation.

[12] In the end the contract consisted of a bundle of documents, which included most relevantly:

(a) the formal agreement which had been part of the tender process; and
(b) documents recording the agreed invoicing procedure as proposed by CPL.

Invoicing arrangements proposed under the formal agreement

[13] The formal agreement contemplated the following steps:

(a) the retailers would order refuse bags from CPL;
(b) CPL was to meet the orders and to invoice the retailers for the total cost ($1.135 per bag);
(c) by the third working day of the following month (that is, month two) CPL was to report to NSCC listing all sales to retailers of refuse bags in the preceding month;
(d) NSCC would pay to CPL the supply costs of the bags (12.5 cents) on the twentieth day of month two;
(e) based on the report issued by CPL (step (c)), NSCC was to invoice CPL for the total amount of the sale proceeds of the refuse bags excluding merchandising/distribution; that is, for $1.115 per bag; and
(f) CPL was to pay NSCC the full invoiced amount by the fifteenth day of the following month (that is, month three).

In the meantime CPL could be expected to collect from the retailers the purchase price ($1.135 per bag).

Invoicing arrangements as eventually agreed

[14] The simpler invoicing arrangements finally agreed upon were:

(a) the retailers would order refuse bags from CPL;
(b) CPL was to meet the orders and to invoice the retailers for the total cost ($1.135 per bag);
(c) by the fifth working day of the following month (that is, month two), CPL was to report to NSCC listing all sales to retailers of refuse bags in the preceding month;
(d) based on the report issued by CPL (step (c)), NSCC was to invoice CPL for the total amount of the sale proceeds ($1.135 per bag) less the agreed merchandising/distribution margin and supply costs (14.5 cents per bag) – in other words, for 99 cents per bag; and
(e) CPL was to pay NSCC's invoice by the twentieth day of the following month.

Whether the payments made by retailers belong in equity to NSCC
Aspects of the contract which point to an agency-trust arrangement

[15] The formal agreement provided that the sale of bags by CPL to the retailers was "on behalf" of NSCC. Consistent with this, the formal agreement provided that "title and risk" passed to NSCC on delivery of the bags to the retailers by CPL. This provision did not correspond to the legal position (as title to the bags passed to the retailers as soon as bags were appropriated to their orders) but, as between NSCC and CPL, is consistent with the idea that CPL was acting as the agent of NSCC when making sales to the retailers. Further, the vast bulk of the price paid by the retailer (99 cents out of $1.135) involved recovery by NSCC of the cost of its collection and disposal services.

Aspects of the contract which point to a debtor-creditor arrangement

[16] Clause 32 of the formal agreement provided that:

> "Nothing in this Agreement shall create a partnership or agency between the parties unless expressly provided."

[17] There is no indication that the parties intended CPL to be required to keep the payments made by the retailers in a separate account. Associated with this is the consideration that the liability of CPL to NSCC was not confined to sums actually received from the retailers; indeed the agreement expressly provided that the terms of credit between CPL and the retailers were not the concern or responsibility of NSCC. CPL was thus to take the risk of retailer default. As well, the payment regimes, both as originally stipulated in the formal agreement and as varied, carried the collorary that CPL would have cash-flow advantages associated with timing differences between its own receipt of payments from the retailers and its obligation to NSCC. That CPL had the advantage of the use of the money in the meantime is not consistent with an agency-trust arrangement in relation to that money.

The approach of Harrison J

[18] Harrison J treated this aspect of the case as turning on whether the contractual arrangements required CPL to keep the funds received from retailers separate. He placed considerable emphasis on the differences between the invoicing arrangement as eventually implemented and contemplated in the formal agreement:

> "**[35]** The agreed invoicing system materially changed that legal structure [that is, as postulated by the formal agreement]. NSCC effectively authorised or licensed CPL to sell the bags directly to the retailers. Sales were on terms and conditions agreed between them. The Council did not participate in those contractual arrangements and never acquired a proprietorial interest in the goods. To the extent that CPL acted on behalf of NSCC, it was for the limited purpose of selling to retailers the right of collection and disposal attaching to the bags for on-sale to the public, and not for the sale of bags which were the company's own property. NSCC was not a principal party to the contracts of sale, it never acquired title to the bags or the fees (I agree with Mr Stewart that the agreed invoicing system rendered the title provision of the tender document inoperative) and it had no enforceable rights against the retailers.
>
> **[36]** By virtue of the invoicing arrangements CPL agreed to underwrite the retailers' payment of the fee to NSCC. It undertook to pay to the Council

by a fixed date an amount equal to the aggregated value of all outstanding fees, irrespective of whether or not it received payment from retailers. So, in accordance with the contractual structure, the retailer received the fee for CPL's benefit and paid accordingly.

[37] There were thus two distinct but interlocking relationships of debtor and creditor. One was between CPL and retailers by virtue of the contract of sale with associated rights of direct recovery. The other was between NSCC and CPL for payment of the fees.

[38] CPL assumed the full transactional risk. In law NSCC assigned or sold its right or interest in the fees to CPL, for which it received payment in the month following submission of invoices. The company was not acting on the Council's behalf when collecting the fees from retailers but for its own benefit as principal. And CPL had no right to a commission on fees recovered; its remuneration lay in the marketing and distribution margin. There is no room within this framework of contracts of sale for a separate relationship of principal and agent between the Council and CPL (see, generally, *Bowstead*, para 1-032)."

[19] He reinforced these conclusions by reference to:

(a) the disclaimer in the formal agreement of the relationship of principal and agent;
(b) the absence from the contractual documentation of any explicit provisions imposing fiduciary obligations on CPL;
(c) the way in which the GST invoices were structured; and
(d) the absence of any requirement in the contract for CPL to hold the fees in a separate account.

Our evaluation

[20] We agree with Harrison J that the critical issue is whether CPL was required to keep the funds received from retailers in a separate account. If that was expressly or implicitly agreed between the parties, then the agency-trust arrangement argument advanced by NSCC must succeed. If not, then that is fatal to NSCC argument.

[21] We are satisfied – and broadly for the reasons given by Harrison J – that the contractual arrangements did not require CPL to hold the money paid by retailers in a separate account.

[22] Commercial firms engaged in a series of running transactions with each other do not usually stipulate for separate banking arrangements to keep funds associated with those transactions separate from the parties' other money. Whether it is right to start with a presumption against an agency-trust arrangement is open to question (compare *Henry v Hammond* [1913] 2 KB 515 at p 521 with *Walker v Corboy* (1990) 19 NSWLR 382 (CA)). And of course in the end it all depends on the circumstances. But it is right to recognise the usual incidents of such running arrangements (and particularly as to the giving of credit) point against a requirement to keep funds separate. See *Paragon Finance plc v D B Thakerar & Co (a firm)* [1999] 1 All ER 400 (CA) at p 416 per Millett LJ:

> ". . . it would appear that the defendant was entitled to pay receipts into his own account, mix them with his own money, use them for his own cash flow, deduct his own commission, and account for the balance to the

> plaintiff only at the end of the year. It is fundamental to the existence of a trust that the trustee is bound to keep the trust property separate from his own and apply it exclusively for the benefit of his beneficiary. *Any right on the part of the defendant to mix the money which he received with his own and use it for his own cash flow would be inconsistent with the existence of a trust. So would a liability to account annually, for a trustee is obliged to account to his beneficiary and pay over the trust property on demand.* The fact that the defendant was a fiduciary was irrelevant if he had no fiduciary or trust obligations in regard to the money. If this was the position, then the defendant was a fiduciary and subject to an equitable duty to account, but he was not a constructive trustee. His liability arose from his failure to account, not from his retention and use of the money for his own benefit, for this was something which he was entitled to do." (Emphasis added.)

[23] We see the arguments which favour a debtor-creditor analysis of the relationship as distinctly more cogent than the considerations going the other way. The structure of the invoicing arrangements as implemented provided for CPL to have the cash-flow advantages associated with the timing differences between its receipt of payments from the retailers and the requirement to pay the balance owing to NSCC (compare the remarks of Millett LJ in the *Paragon Finance* case). As well, there is no necessary connection between actual receipt of payments by CPL and the obligation to pay NSCC. CPL was liable to pay NSCC irrespective of whether it was paid by the retailers.

[24] We recognise that our approach does not give practical effect (at least in the context of this case) to the formal agreement which provided for the notional transfer of title to NSCC and for CPL to sell the bags to retailers "on behalf of" NSCC. Harrison J did not regard these provisions as having the consequence that CPL sold the bags as agents for NSCC. Even if we accepted the contention advanced by Mr Carruthers QC, counsel for NSCC, that the Judge was wrong on this point, we would not have seen this as being of controlling significance. As was recognised by this Court in *Westpac Banking Corporation v Savin* [1985] 2 NZLR 41 at p 49, there can be agency arrangements where the agent who sells the goods of another is not required to keep the proceeds of sale separate and where the obligation to account for those proceeds of sale is thus on a debtor-creditor basis. At the most, the provisions relied on by NSCC provide for CPL to sell the bags as agent for NSCC. There is no stipulated requirement for CPL to receive payments for the bags as the agent of NSCC. If this had been intended, either the disclaimer of agency in cl 32 of the agreement would have been differently expressed or the agreement would have made express provision for CPL to be the agent of NSCC in respect of the payments. And even more significantly, for the reasons already given at paras [22] and [23] above, it is clear that separate banking arrangements were not required, a consideration which is conclusive against the argument that the proceeds of sale were to be held on trust for NSCC.

[25] We conclude by noting that if there is some incoherence to the contract as we interpret it, this is unsurprising given the imprecision of the formal agreement which went to tender and the subsequent tacking on of an invoicing arrangement which differed from that originally contemplated.

The PPSA issue

The issue

[26] Under our interpretation of the contractual arrangements, the PPSA point does not require determination. But like Harrison J, for the sake of completeness, we think it right to express a view.

[27] This view is necessarily premised on the assumption that the contractual arrangement between CPL and NSCC required CPL to receive payments from retailers as agent (and trustee) for NSCC. The question we address in this section of the judgment is whether the rights of NSCC under such an arrangement would be "a security interest" as defined in s 17(1) of the PPSA. It is common ground that if the postulated interest was a "security interest", it would be postponed to the security under which the receivers were appointed; this because it was never perfected in the manner contemplated by the PPSA.

The definition of "security interest"

[28] Section 17(1) of the PPSA relevantly provides:

> **17. Meaning of "security interest" –** (1) In this Act, unless the context otherwise requires, the term **security interest** –
>
> (a) Means an interest in personal property created or provided for by a transaction that in substance secures payment or performance of an obligation, without regard to –
>
> (i) The form of the transaction; and
>
> (ii) The identity of the person who has title to the collateral; and
>
> (b) Includes an interest created or provided for by a transfer of an account receivable or chattel paper, a lease for a term of more than 1 year, and a commercial consignment (whether or not the transfer, lease, or consignment secures payment or performance of an obligation).

Evaluation

[29] Mr Carruthers argued that where an individual has only the proprietary interest of a beneficiary under a trust, that alone necessarily cannot amount to a security interest. We agree that this is so. A security interest under s 17(1) must "in substance [secure] payment or performance of an obligation". The interest held by a beneficiary does not secure any obligation independent of those arising pursuant to the trust.

[30] The difficulty with this argument in the context of this case is that if the arrangement between the parties was as postulated, the trust obligation of CPL with respect to money received was not coterminous with its primary obligation to NSCC. This is because that obligation involved a requirement that CPL pay NSCC in respect of bag sales irrespective of whether the retailers had paid CPL. So assuming that CPL was required to keep in a separate bank account what was paid by the retailers, the associated trust obligations did not exhaust the obligations of CPL to NSCC.

[31] In effect CPL would have had a contractual debtor-creditor obligation to pay NSCC in respect of bags sold, not just to account to NSCC for money it received on NSCC's behalf and held as a trustee. In that context, the only purpose of stipulating for a trust obligation in relation to money paid by the

retailers would be to provide security against the possibility of contractual default by CPL. Such trust obligation would properly be regarded as a security interest within the meaning of s 17.

Disposition

[32] The appeal is dismissed. NSCC is to pay the respondents costs for a standard appeal on a band A basis and usual disbursements.

Appeal dismissed.

Solicitors for the Council: *Wilson Harle* (Auckland).
Solicitors for the receivers: *Buddle Findlay* (Auckland).

Reported by: Alana Sharee MacLean, *Barrister and Solicitor*