IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV 2009-404-001500

	BETWEEN	COMPASS CAPITAL LIMITED Applicant
	AND	THE NEW ZEALAND GUARDIAN TRUST COMPANY LIMITED Respondent

Hearing: 17 March 2009

Appearances: B D Gray QC and C T Walker for Plaintiff
M J Tingey and J C Caird for Defendant

Judgment: 19 March 2009

JUDGMENT OF COOPER J

This judgment was delivered by Justice Cooper on
19 March 2009 at 3.30 p.m., pursuant to
r 11.5 of the High Court Rules

Registrar/Deputy Registrar
Date:

Solicitors:
Bell Gully, PO Box 4199, Auckland 1140
Gilbert Walker, PO Box 1595, Shortland Street, Auckland

[1] The plaintiff in this proceeding, commenced on 17 March 2009, has made an interlocutory application on notice for an injunction restraining the defendant from appointing receivers over the plaintiff.

[2] An urgent hearing was arranged before me on the afternoon of 17 March. Some aspects of the plaintiff's claim rested on propositions that were novel, and without relevant authorities to which counsel were able to refer, and I indicated that I would take time to consider the position. In the meantime, the defendant undertook not to proceed with the intended appointment of receivers pending the delivery of this judgment.

[3] I add the further preliminary observation that while Mr Tingey and Mr Caird were in a position to present argument on the application which had been very recently served on them, they had not had time to obtain affidavit evidence. Mr Tingey, during the course of argument, made some submissions on factual matters from the Bar and also handed up some documents. There was no objection to this course by Mr Gray and it was the only practical way of proceeding.

[4] The defendant's preparedness to argue the matter at short notice was subject to the reservation that if I formed the view that interim relief should be granted, then it should only be for a very short period of time and subject to the allocation of an urgent priority fixture.

Background

[5] In its statement of claim, the plaintiff pleads that the defendant entered into a Trust Deed dated 19 May 2006 ("the Trust Deed") pursuant to which the defendant agreed to act as the trustee for the holders of Secured Bonds issued by the plaintiff. The plaintiff ceased issuing securities in August 2007. As explained in the affidavit of Ian Wayne Gladwell, sworn on 17 March 2009 in support of the application for interim injunction, the plaintiff has been realising its assets and repaying holders of the Secured Bonds.

[6] Mr Gladwell is the Executive Director of the plaintiff. He deposed that, as at 30 June 2007, the plaintiff had issued "senior Secured Bonds" with a value of $19,676,717.09 and "subordinated Secured Bonds" with a value of approximately $2 million. Since then, Secured Bond holders have been repaid approximately $7.33 million. Currently, the plaintiff owes $13,731,051.13 to senior Secured Bond holders and $617,452 to subordinated Secured Bond holders.

[7] The plaintiff has three principal assets. First, there is an advance in respect of a development known as "Bendemeer". The advance has no current value. The plaintiff has an interest in a policy of indemnity insurance which provides indemnity for losses up to $3.5 million in respect of that advance.

[8] Secondly, there is an advance to a development known as "Pacific Palms" which is secured by second mortgage and has a present value of approximately $6.5 million.

[9] There is a further advance, in respect of a development known as "Hermes" which is secured by first mortgage. The present value of the advance is said to be about $3.5 million. As at August 2008, the value of the security exceeded the value of the advance.

[10] In addition, the plaintiff has cash of approximately $1 million. According to Mr Gladwell, if all of the assets are able to be realised, the plaintiff will be able to repay all of the principle owed to Secured Bond holders.

The threat to appoint receivers

[11] Attached to Mr Gladwell's affidavit was a letter written by the defendant as the trustee for the bond holders. The letter, dated 16 March 2009, was in the following terms:

> **Trust Deed dated 17 May 2006**
>
> 1. We refer to the Trust Deed dated 19 May 2006 ("the Trust Deed") between Compass Capital Limited ("Compass") and The New Zealand Guardian Trust company Limited ("the Trustee").

2. There have been a number of Events of Default pursuant to clause 10.1(a) of the Trust Deed which are continuing, in that Compass has failed to pay:

    a. the interest on all Senior Bonds since 31 July 2008; and

    b. all principal on Senior Bonds due from and including 31 July 2008 to date.

3. Pursuant to clause 11.1(a) of the Trust Deed, the Trustee hereby declares the whole of the moneys under the Secured Bonds have become immediately to be due and payable. Unless Compass pays the whole of the moneys (which includes the principal moneys and interest payable on the Secured Bonds) by 4pm on Tuesday 17 March 2009, the Trustee intends to exercise its power under the Trust Deed to appoint Receivers over Compass without further notice.

[12] The plaintiff asserts that the appointment of receivers would in fact prejudice the interests of the Secured Bond holders. Mr Gladwell states in his affidavit that the "Pacific Palms" developer has an unconditional contract to refinance its borrowings through an AAA-rated lender. The refinancing would enable the plaintiff to recover all of its advance and pay this to Secured Bond holders. Although there have been delays in settlement (the refinancing was expected to take place late last year) the plaintiff has been advised by the intending lender that the bonds which it needs to issue to raise funds to make the refinancing advance have now been issued, and that the sale of the bonds is imminent. The lender expects that the bonds will be sold on or before 31 March 2009. Mr Gladwell expresses the opinion that there is nothing that the plaintiff or a receiver could do to accelerate sale of the bonds or refinancing of the advance. In the meantime, the plaintiff maintains that the appointment of receivers would likely lead to other charge holders enforcing their securities in respect of the "Pacific Palms" project with the result of frustrating repayment of the plaintiff's advance and forestalling any recovery under the second mortgage.

[13] The plaintiff has an insurance policy indemnifying the first $3.5 million lost in respect of any particular advance. Mr Gladwell referred to the possibility that the policy might respond if Compass were not repaid in respect of the "Pacific Palms" advance. However, a claim had been made under the policy in respect of the "Bendemeer" advance and Mr Gladwell said that experience in respect of that claim suggested that the underwriters would need to be satisfied "to a very high degree" that indemnity was available before they would pay out. He expressed the concern

that if receivers were appointed, the underwriters would argue that the plaintiff, through its agent the Trustee, had prejudiced recovery of the "Pacific Palms" advance and thereby foregone indemnity.

[14] Mr Gladwell also gave evidence that on receipt of the letter of 16 March, he had telephoned brokers representing secured bond holders who held 66.8 per cent of the value of all secured bonds. Fifteen of the sixteen brokers said that their clients would be opposed to such an appointment. Some indicated that they would want a meeting of secured bond holders called to consider the issue. Finally, Mr Gladwell deposed that he was unaware of any prejudice that would be suffered by the secured bond holders, or by the Trustee, if the appointment of receivers were delayed to allow secured bond holders to consider and vote on the issue.

[15] I note in passing that, although an alternative form of interim relief was sought in which the order made would have effect pending a meeting of secured bond holders called to consider whether receivers should be appointed, Mr Gray did not pursue an order in those terms. Rather, he indicated that the plaintiff would be content if the order sought remained in effect down to "the end of April or the end of March".

The Trust Deed

[16] A copy of the Trust Deed was attached to Mr Gladwell's affidavit. It is not necessary to mention all of its provisions. However, the following should be noted.

[17] First, Recital B recorded that the Trustee (the defendant) had agreed to act as the Trustee for the holders of Secured Bonds pursuant to the Securities Act and as a security trustee on the terms set out in the Deed.

[18] Clause 4.1 was in the following terms:

> **4.1 Security Interest in personal Property**
>
> (a) **Grant of Security Interest and Charge**: The Company:

(i) grants to the Trustee (for itself and on behalf of Holders) a first-ranking Security Interest in all of its Personal Property (both present and future) to secure the payment of the Bond Obligations; and

(ii) charges in favour of the Trustee (for itself and on behalf of Holders) by way of a floating Charge all of its Other Property (present and future) to secure the payment of the Bond Obligations.

(b) **Liberty to Deal**: Subject to clauses 5, 6 and 7, until the Enforcement Date, the income, proceeds or other funds comprising, relating to or derived from the Charged Assets may be applied by the Company in the ordinary course of its business and the Company shall be free to transfer, sell, assign, dispose of or deal in the Charged Assets in the ordinary course of its business or as contemplated by any of the Transaction Documents at its complete and unfettered discretion and any property comprising part of the Charged Assets so dealt with by the company shall be deemed to be released from the Security Interest or the Charge granted by the Company under clause 4.1 without any further action or consent on the part of the Trustee.

(c) **When Floating Charge over Other Property becomes a Fixed Charge**: Any floating Charge created by this Deed in relation to Other Property will become a fixed Charge automatically, without the need for any notice or action by the Trustee, immediately prior to, or if that is not legally effective, contemporaneously with the occurrence of any Event of Default.

(d) **Security Trust**: The Trustee, by execution and delivery of this Deed, acknowledges that it shall hold the Charge in the Charged Assets created by this Deed, in trust, for the benefit of the Holders, on the terms and subject to conditions contained in this Deed.

[19] "Events of Default" were defined in clause 10.1. It is not necessary to set out all the provisions of this clause. However, defaults in the payment of money on the due date under the Deed were relevant events of default. It was common ground that such events have occurred and in particular, the plaintiff defaulted on payments due in July 2008 and subsequently. Clause 12.1 of the Trust Deed empowered the Trustee in its discretion to appoint a receiver or receivers "at any time after the Enforcement Date". The "Enforcement Date" was defined in clause 1.1 of the Deed as being "the day on which the Trustee determines to exercise its Enforcement Powers". The "Enforcement Powers" were defined in clause 11.1. Such a power was exercised in the 16 March 2009 letter, pursuant to clause 11.1(a), which authorised the Trustee to "declare the whole of the Moneys to have become

immediately due and payable whereupon the Moneys shall forthwith become immediately due and payable".

[20] In the circumstances, there was no dispute that the defendant had power to appoint a receiver. The question raised by the plaintiff's claim is whether that power can properly be exercised.

Basis of the Plaintiff's claim

[21] The plaintiff's claim rests on the fact that the effect of clause 4.1(a) of the Trust Deed is to create a Security Agreement under the Personal Property Securities Act 1999. Section 25(1) of that Act provides:

> All rights, duties, or obligations that arise under a security agreement or this Act must be exercised or discharged in good faith and in accordance with reasonable standards of commercial practice.

[22] Essentially, the plaintiff argues that the appointment of receivers can only have an adverse effect on the interests of the plaintiff and of the bond holders whom the Trustee represents. Because the appointment would have those consequences, effectively foreclosing opportunities for recovery which presently exist, it is argued that the appointment cannot be "in accordance with reasonable standards of commercial practice".

The Defendant's response

[23] Mr Tingey, for the defendant, opposed the grant of relief on a number of grounds. First, he maintained that absent an allegation of bad faith, the appointment of receivers was effectively unreviewable and simply governed by s 6 of the Receiverships Act 1993. Section 6(1) enacts:

> A receiver may be appointed in respect of the property of a person by, or in the exercise of a power conferred by, a deed or agreement to which that person is a party.

[24] Here, the receiver had simply been appointed in exercise of the power contained in clause 12.1 of the Trust Deed. He explained that the defendant was, of

course, fully aware of the various issues that Mr Gladwell had raised. Its commercial judgment nevertheless led it to conclude that the appointment of receivers was warranted. In substantial part, that was because the defendant had lost confidence in Mr Gladwell as the executive director and sole employee of the plaintiff.

[25] That loss of confidence arose in part as a result of a payment of $90,000 that Mr Gladwell had procured to himself from the plaintiff. There was no dispute that a payment of $90,000 was payable under Mr Gladwell's employment contract once he became redundant. However, it appeared that Mr Gladwell was entitled to the payment only when he became redundant on 31 March 2009, and he was not entitled to the payment at this stage.

[26] However, there had also been relevant correspondence between the defendant and solicitors acting for the plaintiff. In a letter dated 26 September 2008, addressed to Keegan Alexander, the defendant recorded its understanding that Keegan Alexander held certain amounts in its trust account on trust for the plaintiff. The letter noted that an event of default had occurred under the Trust Deed, with the consequence that the Trustee was entitled to exercise its rights to the money held by Keegan Alexander. The letter gave notice of the Trustee's perfected security interest in the money and said that Keegan Alexander should not permit any part of the money to be withdrawn or otherwise liquidated. The letter concluded:

> Please furnish the Trustee with a current statement in respect of the deposit and all accrued interest thereon.

[27] Keegan Alexander replied to the letter on 30 September 2008. The letter stated, amongst other things:

> … we do not consider, at this stage, that we are at liberty to provide the accounting you have requested. Any funds held by us are held on behalf of our client and ethical considerations of trust and confidence prohibit us from disclosing the affairs of our client. We can only suggest that you direct us to attempt to obtain the consent of our client to such disclosure or that you obtain the accounting from our client directly.
>
> Would you also please note that while we will, of course, respect the confidence in your correspondence as against the world at large we are not permitted to withhold information from our client. That being so, you must

> assume and be aware that any communications with us, in respect of the affairs of our client, will be brought to the attention of our client.

[28] Mr Tingey conceded that the defendant had not become aware of the $90,000 payment to Mr Gladwell until 17 March, i.e. the day after the letter of 16 March 2009 declaring the whole of the moneys payable under the secured bonds immediately due, and referring to its intention to appoint receivers under the Trust Deed. However, there was a pre-existing concern based on the exchange of letters between the defendant and Keegan Alexander that money had been taken out of the company's accounts and deposited in a solicitor's trust account with the details deliberately kept from the defendant.

[29] Mr Tingey rejected Mr Gladwell's evidence about implications for the plaintiff's insurance cover. He also submitted that the undertaking as to damages that had been offered was meaningless. The company was effectively insolvent, having owed over $13 million to bond holders since September 2008. In the circumstance that no other form of security had been offered, there was in effect no protection for bond holders under the undertaking.

Discussion

[30] I was not referred to any authorities in which the inter-relationship between s 6 of the Receiverships Act 1993 and s 25 of the Personal Property Securities Act 1999 had been discussed. Mr Tingey referred to (but was not in a position to cite) Canadian authorities which he said suggest that the Canadian legislation equivalent to the Personal Property Securities Act would not justify using s 25(1) to challenge the appointment of a receiver.

[31] Although I have not had the benefit of full argument on the point, I do not consider that it would be appropriate for me to decide this issue against the plaintiff. The language of s 25(1) of the Personal Property Securities Act is very wide. The reference is to "all rights" arising under a security agreement. There is no doubt here that the power to appoint a receiver arises under a security agreement. On the face of it, the words would plainly apply to the appointment of a receiver.

[32] I note, secondly, that s 6(1) of the Receiverships Act 1993 simply provides that a receiver may be appointed in respect of the property of a person under a power conferred by a deed or agreement to which that person is a party. There is nothing in the section which purports to limit or delineate the basis on which such an appointment might be challenged. It is uncontroversial that, at common law, the appointment of a receiver could be challenged because the creditor had acted in bad faith. I am unaware of any suggestion that s 6(1) would remove that common law basis of challenge which is, of course, repeated in s 25(1). I would find it difficult to accept that the good faith obligation should remain, but the wider obligations arising from s 25(1) should somehow be precluded by s 6.

[33] Finally, I note that in Blanchard and Geddye's *The Law of Private Receivers of Companies in New Zealand* (Wellington, LexisNexis 2008) it is observed at 3.03 that:

> Section 25 of the Personal Property Securities Act provides that all rights that arise under a security agreement, which would include the right to appoint a receiver, must be exercised in good faith and in accordance with reasonable standards of commercial practice.

[34] Further, at 3.04, it is said that:

> In other appropriate cases, a secured creditor seeking to appoint a receiver in reliance on a minor default that had been remedied may be found to be acting in contravention of the reasonable standards of commercial practice required by s 25 of the Personal Property Securities Act and Part 5 of the Credit Contracts and Consumer Finance Act 2003.

[35] I agree with that statement of the law.

[36] The questions that then arise, for present purposes, are whether the plaintiff can raise as a serious question to be tried, the issue of whether, on the present facts, the defendant's appointment of receivers would not be in accordance with reasonable standards of commercial practice, whether the balance of convenience favours the grant of interim relief and whether the overall interests of justice would support the grant of interim relief.

[37] On the first question, I consider that the plaintiff faces some serious obstacles. First, there is the fact that the company has been unable to pay its debts as

they fall due for many months, as I understand it since at least September 2008, and its indebtedness is significant. Second, the hopes that the "Pacific Palms" project would be refinanced enabling the plaintiff to recover its investment appear to have been extant for many months. It was Mr Gladwell's evidence that the refinancing was expected to take place shortly after receipt of a report by Korda Mentha (which was produced on the defendant's instructions) in October 2008. However, the settlement was delayed. The cause to which the delay was attributed was the effect of the "credit crisis in the United States". There is a suggestion by the intending funder of the refinancing that it is about to sell the bonds necessary to produce the new funding. There is hearsay evidence that the funder expects the bonds to be sold or completed before 31 March 2009. However, in all the circumstances, and given the ongoing effects of the global credit crisis, I consider the defendant would be justified in taking the view that the prospective refinancing might not eventuate, and in any event should not be a reason to delay the appointment of receivers.

[38] I am not convinced by the plaintiff's argument based on the plaintiff's insurance position. In particular, it is not clear to me why the appointment of receivers should have an effect on the availability of cover for the company and no policy provision to that effect was produced in evidence. Contrary to Mr Gladwell's assertion, the defendant is not the plaintiff's agent.

[39] Added to these considerations is the fact that the payment made by the plaintiff into its solicitor's trust account evidently occurred at a time when it was in default of its obligations under the Trust Deed. The fact of that payment and the failure to disclose its amount and justification to the defendant, present as reasonable grounds on which the defendant could say, as it now does, that it has lost confidence in the management of the company. Whilst such a large debt remains outstanding, I consider that it is perfectly legitimate for the company to adopt that stance and appoint receivers accordingly.

[40] Mr Gray sought to minimise the implications of the fact that it now appears that Mr Gladwell is the recipient of the sum of $90,000 in advance of the date when he would properly be entitled to it. In that respect, he referred to the Korda Mentha report of 30 October 2008. At page 12 of the report it was mentioned that:

> A redundancy payment of $90,000 has been provided for in March 2009 in accordance with Ian Gladwell's employment contract.

[41] Earlier on the same page the report stated that Mr Gladwell would "move to a consultancy basis on 1 April 2009", at an estimated cost of $10,000 per month for three months. Mr Gray maintained that all this was in accordance with Mr Gladwell's employment contract, a copy of which he provided to the Court. However, Mr Tingey's point was that the redundancy payment had not become payable by 17 March, when Mr Gladwell evidently procured it.

[42] The defendant's decision to appoint receivers was made before the defendant knew of the payment to Mr Gladwell and logically ought not to be taken into account in assessing whether the decision to appoint receivers was in accordance with reasonable standards of commercial practice at the time the decision was made. However, the earlier correspondence which I have discussed was sufficient in my view to justify disquiet on the defendant's part in relation to the management of the plaintiff.

[43] It will be for future cases to decide how closely it may be appropriate to examine decisions made to appoint receivers within the framework of s 25 of the Personal Property Securities Act 1999. Whatever test is adopted, however, I am satisfied in the present case, looking at the combination of factors that I have reviewed, that there would be no justification for concluding that the decision to appoint receivers was not made in accordance with reasonable standards of commercial practice. I do not consider that the plaintiff has established a serious question to be tried as to whether the section was breached. In those circumstances, it is unnecessary to go on to consider the balance of convenience and the overall justice of the plaintiff's claim.

Result

[44] The application for injunction is dismissed.

[45] If there is any issue as to costs that cannot be resolved, I will receive memoranda on that issue from the defendant within ten working days and from the plaintiff, five days after that.