IN THE COURT OF APPEAL OF NEW ZEALAND

CA774/2010
[2011] NZCA 672

BETWEEN	GLENMORGAN FARM LIMITED (IN RECEIVERSHIP AND IN LIQUIDATION) Appellant
AND	NEW ZEALAND BLOODSTOCK LEASING LIMITED AND NEW ZEALAND BLOODSTOCK FINANCE LIMITED AND NEW ZEALAND BLOODSTOCK PROGENY LIMITED Respondents

Hearing:	20 and 21 September 2011
Court:	O'Regan P, Chambers and Harrison JJ
Counsel:	M C Black and S W Shin for Appellant P J Morgan QC and R A Edwards for Respondents
Judgment:	20 December 2011 at 2.30 pm

JUDGMENT OF THE COURT

A The appeal is dismissed.

B The appellant must pay the respondents costs for a complex appeal on a band A basis and usual disbursements.

REASONS OF THE COURT

(Given by Harrison J)

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Introduction

[1] The appellant, Glenmorgan Farm Ltd, operated a stud farm. The respondents, subsidiaries of New Zealand Bloodstock Holdings Ltd (individually and collectively Bloodstock), provided funding for Glenmorgan to purchase a breeding stallion called "Generous". Another company, SH Lock and Co Ltd (Lock), also provided Glenmorgan with financial assistance for its commercial operations.

[2] Glenmorgan consistently defaulted on its repayment obligations to Bloodstock, which responded by taking possession of Generous. Glenmorgan then issued proceedings in the High Court, alleging that Bloodstock converted Generous; that there was a failure of consideration; and that Bloodstock had committed other

wrongs. Substantial damages were sought. All claims were dismissed by Potter J,[1] who found also that even if Bloodstock had acted unlawfully Glenmorgan did not suffer loss as a result.

[3] Originally Glenmorgan appealed against the Judge's dismissal of both the conversion and failure of consideration claims. Mr Black's written submissions maintained that position. However, his oral argument was limited to the conversion claim. That course was appropriate: we are satisfied that for the reasons she gave Potter J was correct to dismiss Glenmorgan's failure of consideration claim (see at [17]–[20] below). The remainder of our judgment will be confined to the conversion claim.

[4] Glenmorgan's claim is the third in a series of proceedings among related parties. This Court has determined the central issues arising in the two previous cases – respectively of priority between Bloodstock and Lock[2] and of guarantors' liabilities.[3] As a result the facts relevant to Glenmorgan's appeal are settled. The issues arising are primarily of contractual construction and the application of legal principles.

[5] This appeal raises two primary questions for determination: first, whether Bloodstock committed the tort of conversion; and, second, if so, whether Glenmorgan suffered loss as a result.

Background

[6] Glenmorgan carried on business south of Auckland as an equine bloodstock breeder, purchasing stallions and mares to breed progeny for sale. Bloodstock leases, finances, insures, auctions and sells bloodstock.

[7] In November 1999 Glenmorgan granted Lock a debenture creating a floating charge over its assets to secure advances. In August 2001 Bloodstock purchased

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1 *Glenmorgan Farm Ltd (in rec and in liq) v New Zealand Bloodstock Leasing Ltd* HC Auckland CIV-2008-404-1759, 27 September 2010.
2 *Waller v New Zealand Bloodstock Ltd* [2006] 3 NZLR 629.
3 *Jenkins v New Zealand Bloodstock Leasing Ltd* [2008] NZCA 413.

Generous from Japanese interests and leased him to Glenmorgan under a lease to purchase agreement (LPA1). Glenmorgan promised to pay Bloodstock a total of $3,386,315.23 in three annual instalments and a residual amount scheduled for 31 July 2004. Those events would complete performance of its obligations under LPA1. As lessee, Glenmorgan took immediate possession of Generous and derived income from his stud fees. Glenmorgan was to acquire title to Generous on payment of all monies due under LPA1. In the interim title was to remain with Bloodstock.

[8] Glenmorgan defaulted on its payment obligations under LPA1. On 28 June 2002 the parties restructured their financing arrangement. They entered into a second lease to purchase agreement (LPA2) on terms similar to but in substitution for LPA1. The material differences related to amounts payable and an acceleration of the termination date to 28 March 2004. On that event, title to Generous was to pass to Glenmorgan.

[9] On 1 May 2002 the Personal Property Securities Act 1999 (the PPSA) came into force. However, Bloodstock took no steps to register a financing statement in respect of its security interest under either LPA1 or LPA2. Its security interest was therefore unperfected. In *Waller v New Zealand Bloodstock Ltd*[4] this Court held that Lock's security interest in Generous as after-acquired property was perfected in terms of the PPSA from 1 May 2002. Thus Lock obtained priority from that date over Bloodstock's security interest which was never perfected by registration.[5]

[10] On 28 November 2002 Glenmorgan paid $1 million of the instalment of over $1.3 million due under LPA2. But no further payments were made. On 22 August 2003 the parties again restructured Glenmorgan's indebtedness, this time through a Refinancing Agreement (RA) and a Contract for Current Advances (CCA). Four members of the Jenkins family guaranteed Glenmorgan's performance of its new obligations. All were either shareholders or former shareholders in Glenmorgan. Litigation subsequently ensued between Bloodstock and those parties, culminating in this Court's decision in *Jenkins v New Zealand Bloodstock Leasing Ltd*.[6]

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4 *Waller v New Zealand Bloodstock Ltd* [2006] 3 NZLR 629 (CA).
5 PPSA, s 17(1)(b); *Waller* at [51] and [54].
6 *Jenkins v New Zealand Bloodstock Leasing Ltd* [2008] NZCA 413.

[11] The RA recited Glenmorgan's indebtedness to Bloodstock at $2,652,545 and its undertakings to make successive payments of $1,000,000 on 28 November 2003 and $350,000 on 28 March 2004;[7] these amounts were shortfalls of $372,795 and $237,142 respectively on the amounts actually owing under LPA2. The parties agreed that, providing Glenmorgan paid the two instalments, Bloodstock would advance the shortfalls under the CCA.[8] Furthermore, notwithstanding that the CCA provided for repayment on demand, Bloodstock agreed not to exercise that right and seek early repayment of monies due, subject to Glenmorgan paying the two sums of $1,000,000 and $350,000 on the due dates together with $1,000,000 on 28 November 2004 and the balance owing under the CCA by 28 March 2005.[9]

[12] The whole amount due under the CCA became immediately payable if Glenmorgan defaulted on these obligations. In that event, Bloodstock was entitled to exercise any of its rights under LPA2, the CCA, the RA or at law.[10] The CCA referred specifically to rights arising under the PPSA, a point to which we shall return (see at [45]–[50] below). In this respect, LPA2 provided that if Glenmorgan failed to perform any of its provisions Bloodstock was entitled at its option to terminate LPA2 and take possession of Generous.[11]

[13] Glenmorgan failed to make the two payments due under LPA2 on 28 November 2003 and 28 March 2004. Nevertheless, on the latter date Bloodstock made advances under the RA and CCA equal to the amounts due. By agreement they were applied to discharge Glenmorgan's payment obligations under LPA2. Bloodstock effected these advances by internal accounting entries, offsetting the discharge of Glenmorgan's obligations under LPA2 against a corresponding increase in its indebtedness under the CCA. The total amount advanced by Bloodstock remained unchanged.

[14] On 25 June 2004 Bloodstock requested Glenmorgan to pay an overdue amount of $1,132,366 by 5 July 2004. On 6 July, in the absence of a reply to its

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7 Cl 2(b), RA.
8 Cl 3(a) and (b), RA.
9 Cl 5(a), RA.
10 Cl 5(b), RA.
11 Cl 6(a).

request, Bloodstock's solicitor gave Glenmorgan notice of its breach of obligations under the existing contracts; and of Bloodstock's termination of the RA and the CCA. As a result, Bloodstock advised the sum of $2,400,251 was due and owing as at 30 June, and it intended to take possession of Generous.

[15] On 7 July 2004 Bloodstock took possession of Generous when it returned from servicing mares in the northern hemisphere. The stallion was taken to Westbury Stud, also south of Auckland, for the southern hemisphere breeding season. On 25 July Lock appointed receivers of Glenmorgan. In March 2005 the company was wound up.

[16] Lock and Bloodstock co-operated in managing Generous' servicing arrangements. Lock received the income after Bloodstock took possession. In June 2005 the receivers appointed by Lock sold Generous for $1,013,153. The proceeds were applied in reduction of Glenmorgan's indebtedness to Lock.

High Court

[17] Glenmorgan's first claim alleged a total failure of consideration. Issues were raised about the extent of its rights to Generous under the various agreements and the consequences of Bloodstock's failure to perfect its security interest in Generous.

[18] Potter J held that Glenmorgan acquired title to Generous on paying all monies owed under LPA2 with funds made available under the CCA.[12] LPA2 was thereby discharged and extinguished.[13] Despite some dispute over whether the full amount owing under LPA2 was paid, the Judge concluded that there was accord and satisfaction. Therefore, determination of the parties' rights under the RA and CCA became the real issue.

[19] Generous together with seven other brood mares comprised the collateral for Bloodstock's advances made under the CCA. While that instrument conferred on

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12 At [46], adopting the judgment of Winkelmann J in *New Zealand Bloodstock Leasing Ltd v Jenkins* (2007) 3 NZCCLR 811 (HC); affirmed in *Jenkins v New Zealand Bloodstock Leasing Ltd* [2008] NZCA 413.

13 At [49].

Bloodstock the benefit of a security interest in Generous and the mares, Lock's priority over the stallion was maintained through its perfected security interest under its debenture. If Glenmorgan had fulfilled its obligations under the RA and CCA, then its title to Generous would have been subject only to Lock's debenture. That would have been the case even if Bloodstock had registered its security interest under LPA1 or LPA2.[14] Moreover, Bloodstock could not have done anything to free Glenmorgan of Lock's security interest in its assets.[15]

[20] In those circumstances, Potter J concluded, "Glenmorgan got nothing less than it had contracted for".[16] There was no failure of consideration. In reaching that conclusion, the Judge took particular note of two CCA provisions: cl 8(b) whereby Glenmorgan represented that it owned Generous free of "all prior security interests"; and cl 8(h) whereby Glenmorgan warranted that the collateral was not subject to "security of any kind whatsoever". The prior existence of Lock's debenture, the Judge found, meant Glenmorgan breached both provisions from inception.[17]

[21] Those breaches also proved decisive against Glenmorgan's alternative claim for trespass or conversion arising from Bloodstock taking possession of Generous. In dismissing this cause of action Potter J again adopted[18] Winkelmann J's reasoning in *Jenkins*, which can be summarised as follows:[19]

(a) Bloodstock had no recourse to its rights under LPA2 as that instrument was at an end and thus it had to rely on its rights under the CCA.

(b) By cl 10(a), the CCA terminated on Glenmorgan's breach. In that event Bloodstock would "have all the rights available at law including if applicable those under the PPSA relating to the security interest in the collateral".

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14 At [72].
15 At [72].
16 At [76].
17 At [63]–[64].
18 At [89].
19 Those reasons in turn are summarised by Potter J at [82]–[88].

(c) Bloodstock had no statutory rights to enforce its security under the PPSA because s 109 of that Act, as it stood, only gave secured parties "with priority over all other secured parties" the right to take possession and sell the security.[20]

[22] Potter J dismissed Glenmorgan's claim on different grounds, noting:

> [90] To be successful in a claim for conversion against [Bloodstock], Glenmorgan would have to be able to show that at the time of the conversion it had possession, or a right to immediate possession of Generous. However, it was seriously in default under the [CCA]. Not only had it breached clause 8(b) and clause 8(h) ... by granting the prior security interest to Lock, but it had defaulted in making the payments due to [Bloodstock]. Under clause 5(b) of the [RA] if Glenmorgan failed to make payments on due date (which it indisputably did) the whole of the amount due under the [CCA] forthwith became due and payable and [Bloodstock] was entitled to exercise any or all of its rights at its discretion under LPA2, the [CCA], the [RA] or at law. And under clause 10(a) of the [CCA], the agreement was terminated.

[23] While it was accepted that Glenmorgan had possession in fact,[21] Potter J concluded:

> [91] Glenmorgan had no continuing rights to possession of Generous. *Harris v Lombard New Zealand Ltd*,[22] *Aubit Industries Ltd v Cable Price Corp Ltd*[23] are both hire purchase cases where it was held that the debtor could not sustain a claim of conversion against the creditor when at the time of repossession it was in default of payments due under the hire purchase agreement.
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> [92] While the repossession of Generous by [Bloodstock] was unlawful as against Lock because of the provisions of s 109 as it then stood, it was not wrongful as against Glenmorgan.

[24] In any event, Potter J found that Glenmorgan could not have established any loss as the proceeds of Generous' sale were applied in reduction of Glenmorgan's indebtedness to Lock. The Judge therefore found it unnecessary to consider evidence of the stallion's value at the time Bloodstock took possession of it.[24]

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20 Section 109 of the PPSA was amended by s 364(1) of the Property Law Act 2007, which omitted the quoted words with the effect that any secured party may unambiguously repossess and sell the security.

21 At [6], [62] and [73].

22 *Harris v Lombard New Zealand Ltd* [1974] 2 NZLR 161 (SC).

23 *Aubit Industries Ltd (in rec and in liq) v Cable Price Corp Ltd* (1994) 5 NZBLC 103,395 (CA).

24 At [93].

Conversion

(a) Principles

[25] Glenmorgan's sole remaining ground of appeal on liability is that Potter J erred when dismissing its claim in conversion.

[26] The constituent elements of the tort of conversion have been described in many authoritative ways. We adopt for these purposes Lord Nicholls' statement for the majority in *Kuwait Airways Corp v Iraqi Airways Co (Nos 4 & 5)*:[25]

> 39 … Conversion of goods can occur in so many different circumstances that framing a precise definition of universal application is well nigh impossible. In general, the basic features of the tort are threefold. *First, the defendant's conduct was inconsistent with the rights of the owner* (or other person entitled to possession). Second, the conduct was deliberate, not accidental. Third, the conduct was so extensive an encroachment on the rights of the owner as to exclude him from use and possession of the goods. The contrast is with lesser acts of interference. If these cause damage they may give rise to claims for trespass or in negligence, but they do not constitute conversion.
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> (Our emphasis.)

[27] In the same case, Lord Steyn formulated this slightly different description of the tort:

> 119 Despite elaborate citation of authority, I am satisfied that the essential feature of the tort of conversion, and of usurpation under Iraqi law, *is the denial by the defendant of the possessory interest or title of the plaintiff in the goods*: see [Stephen Todd (ed) *The Law of Torts in New Zealand* (3rd ed, Brookers, Wellington, 2001) at [11.3]] for an illuminating discussion. When a defendant manifests an assertion of rights or dominion over the goods which is inconsistent with the rights of the plaintiff he converts the goods to his own use. ...
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> (Our emphasis.)

[28] The argument before us focussed on the first of the three elements identified by Lord Nicholls in the *Kuwait Airways* case. To satisfy that first element in

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[25] *Kuwait Airways Corp v Iraqi Airways Co (Nos 4 & 5)* [2002] UKHL 19, [2002] 2 AC 883; adopted by this Court in *JS Brooksbank and Co (Australasia) Ltd v EXFTX Ltd (in rec and liq) formerly known as Feltex Carpets Ltd* [2009] NZCA 122, (2009) 10 NZCLC 264,520 at [21]–[22].

circumstances when competing rights are in dispute, the party claiming conversion of property must prove that its possessory right is superior to the defendant's right.[26] In other words, it is not enough to assert a bare right of possession against a defendant asserting the same right. The claimant must show both that it has a right and that its right trumps the defendant's right.

[29] Before proceeding further in our analysis, we note two points. First, we accept Mr Black's submission that Glenmorgan was lawfully in possession of Generous on 7 July 2004; to the extent that Potter J found to the contrary (see at [23] above), we respectfully disagree. That conclusion is sufficient to give Glenmorgan standing to sue. The enquiry thus shifts to an examination of whether Bloodstock had a right as security holder to seize Generous and, if so, whether that right was superior to Glenmorgan's possessory right. In practice the answer to the first question will dictate the answer to the second; if both are in the affirmative Bloodstock's action was lawfully justified.[27]

[30] Second, while Bloodstock took possession of Generous on 7 July 2004, it did not sell the stallion. Bloodstock later surrendered possession of Generous to Glenmorgan's receivers. In turn they sold the stallion in June 2005. Thus, any consideration of the lawfulness of Bloodstock's powers must be limited to its act of taking possession. This factor must be borne in mind throughout. Much of Mr Black's argument proceeded on the implicit but mistaken premise that Bloodstock was responsible for permanently depriving Glenmorgan of Generous.

(b) Defaults

[31] Potter J's unchallenged findings on two critical defaults by Glenmorgan provide the factual setting for our inquiry:

(a) On 22 August 2003, when the parties entered into the RA and CCA, Generous was already subject to a security interest in favour of Lock. So, from the inception of both instruments, Glenmorgan was in breach

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[26] Sarah Green and John Randall *The Tort of Conversion* (Hart Publishing, Oxford, 2009) at 75, 95–103.

[27] See *Cuff v Broadlands Finance Ltd* [1987] 2 NZLR 343 (CA) at 346.

of its obligations to Bloodstock. A range of remedies was available. On that event all outstanding monies became due and payable.

(b) On 5 July 2004 Bloodstock was entitled to exercise its remedies under the RA and CCA for Glenmorgan's default in payments due of $2.4 million. Glenmorgan has not cross-appealed Potter J's judgment on Bloodstock's counterclaim of $2.22 million.

(c) Contractual rights

(i) Parties' intentions

[32] What then were the contractual consequences of both defaults? In particular, did the parties agree that Bloodstock would be entitled to take possession of Generous if either default occurred? While neither the RA nor the CCA expressly authorised Bloodstock to seize Generous, can that right nevertheless be read into either contract?

[33] The starting point is to assess objectively the parties' intentions when they entered into the RA and the CCA on 22 August 2003, consistent with the commercial purpose and business commonsense of the arrangements[28] and by reference to the circumstances as they then existed. In 2001 Bloodstock had provided Glenmorgan with a facility to purchase Generous. By 2003 Glenmorgan was in substantial default: to rectify it the parties agreed to restructure their arrangement – effectively to extend time for repayment on different terms.

[34] The rationale for both transactions was to assist Glenmorgan's acquisition of Generous. In keeping with orthodox financing practice, the parties would be expected to give the financier a security interest in the asset being purchased, with associated rights of taking possession and sale on default. Otherwise the financier would have no effective right of recourse other than liquidation of the borrower. LPA2 had expressly provided those rights. It may be thought unlikely that, when

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[28] *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC 5, [2010] 2 NZLR 444 at [22] per Tipping J.

later restructuring the arrangement, Bloodstock would agree to forego its security rights without a sound reason. An examination of the contractual instruments is required.

(ii) The RA

[35] Mr Morgan QC submits that as at 22 August 2003 cl 5(b) of the RA preserved Bloodstock's existing security rights under LPA2. He says that cl 5(b) gave Bloodstock a greater possessory right to Generous than Glenmorgan once the latter defaulted on its specific payment obligations under cl 5(a).

[36] Clause 5(b) entitled Bloodstock to "exercise any or all of its rights ... under [LPA2] ..." if Glenmorgan failed to pay either of the instalments of $1 million and $350,000 due respectively on 28 November 2003 and 28 March 2004 (see at [11] and [12] above). While that payment obligation was imposed by cl 5(a) of the RA, cl 1(b) and cl 2 of that instrument recited that the sums were due and payable under LPA2. As we have noted (see at [13] above), on 28 March 2004 Bloodstock advanced the funds to Glenmorgan necessary to pay the instalments due under LPA2. The advances were treated as being made under cl 2(b) of the CCA facility. Their effect as from 28 March 2004 was to shift the burden of Glenmorgan's indebtedness from a liability under LPA2 to one arising under the CCA.

[37] Bloodstock's powers under cl 5(b) of the RA were expressly limited to Glenmorgan's failure to pay the two instalments due under LPA2 referred to in cl 5(a). By advancing funds to Glenmorgan for that purpose, Bloodstock effectively enabled it to remedy any breaches of cl 5(a) and discharge its obligations under LPA2. Bloodstock could not after 28 March 2004 rely on cl 5(b) to justify its taking possession of Generous.

[38] Winkelmann J aptly summarised the position in *Jenkins* as follows:[29]

> [55] ... The advances made pursuant to the refinancing were intended to be, and were applied over time to performance of Glenmorgan's payment obligations under LPA2. Glenmorgan agreed to the provision of separate

[29] *New Zealand Bloodstock Leasing Ltd v Jenkins* (2007) 3 NZCCLR 811 (HC).

> security for the advances made by reason of the refinancing. What was plainly envisaged was that LPA2 would proceed through to completion, Glenmorgan would acquire title in Generous, and [Bloodstock] would have a security interest in Glenmorgan's rights to Generous, securing the amounts outstanding under the [CCA]. I am satisfied that this negatives any intention to retain the LPA2 security interest after payment of all amounts outstanding under it with advances under the [CCA]. The LPA2 purchase money security interest was therefore extinguished by March 2004.
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> …
>
> [60] The parties to the [CCA] clearly intended to grant a security interest in Generous as security for the advances made under that contract, and I consider that the provisions of that contract were sufficient to do so, although not a purchase money security interest, and not a perfected security interest due to the absence of registration.

[39] However, that is not the end of the road for Bloodstock. Counsel did not address argument before us, or apparently before Potter J, on cl 5(c) of the RA. That provision materially stated:

> ... a breach of any of the provisions of [LPA2, the CCA and the RA] shall entitle [Bloodstock] to exercise any or all of its rights under all or any such agreement.

[40] Clause 5(c) can properly be construed, we think, as the parties' agreement on 22 August 2003 to provide Bloodstock with the same default right available under the two related contracts – LPA2 and the CCA. They apparently adopted a shorthand drafting practice to avoid repetition of the lengthy security provisions in LPA2. The parties plainly intended that the three concurrent security documents should be read together except to the extent that material provisions were inconsistent. The two instruments later in time – the RA and the CCA – referred frequently and expressly to LPA2. There is no inconsistency in construing cl 5(c) of the RA as incorporating an express right of enforcement from a related contract which was critical to the protection of the lender's security in the primary collateral.

[41] We are concerned solely with Bloodstock's right to take possession. Under cl 6(a) of LPA2 that power was triggered if Glenmorgan failed to perform any of LPA2's provisions. In our judgment the same right to take possession was incorporated with the necessary changes, being a failure to perform any of the provisions of the RA and the CCA, to be read into cl 5(c) of the RA.

[42] It follows that Bloodstock had a contractual right to take possession of Generous if Glenmorgan breached the CCA at any time after 22 August 2003. Glenmorgan was incontestably in default of its obligations under the CCA when it failed to meet Bloodstock's demand for payment on 25 June 2004, if not earlier. That right was not affected by Glenmorgan's discharge of LPA2 on 28 March 2004.

[43] Bloodstock's right was reinforced by these provisions of the CCA:

(a) In consideration for Bloodstock's entry into the facility and the advances made under it Glenmorgan granted a security interest in terms of the PPSA in nominated collateral including Generous and agreed to give every assistance to enable Bloodstock to register a financing statement under that Act.[30]

(b) Glenmorgan agreed that its creation of a charge or encumbrance over the collateral without Bloodstock's prior written consent constituted a breach for which the lender acquired all rights available to it at law.[31]

(c) Glenmorgan warranted that it had good title to Generous free of all prior security interests, charges or encumbrances;[32] that Generous was not subject to any such charge; and that while any monies remained unpaid under the facility it would not permit such a charge.[33] A breach or breaches of these warranties entitled Bloodstock to exercise rights of termination limited to charging penalty interest and recovering costs associated with the default.[34]

(d) However, the agreement then stated:[35]

> If [Glenmorgan] shall fail to pay any monies owing by [it] to [Bloodstock] or if there is any breach of the terms hereof, then this Agreement shall forthwith be terminated and [Bloodstock] shall have all of the rights available at law including if applicable

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30 Cl 6(a) and (b), CCA.
31 Cl 6(c), CCA.
32 Cl 8(b), CCA.
33 Cl 8(h) and (i), CCA.
34 Cl 8(j), CCA.
35 Cl 10(a), CCA.

> those under the [PPSA] relating to the security interest in the Collateral.

[44] In combination, the relevant provisions of the RA and CCA show that when the parties contracted on 22 August 2003 they were operating on the premise that, first Bloodstock had and would continue throughout to have a first ranking security interest in Generous; and, second, in that capacity Bloodstock would be entitled to enforce its security by exercising all rights to take possession whether available at law – that is, by contract – or by statute if Glenmorgan defaulted. The statutory rights "relating to the security interest in the collateral" derived expressly from s 109 of the PPSA.

(iii) The PPSA

[45] The CCA was a security agreement.[36] Glenmorgan granted Bloodstock a specific security interest in Generous by creating an interest in the stallion under a transaction which in substance secured payment or performance of obligations.[37] Bloodstock's security interest was never perfected by registration.[38] Nevertheless it remained by agreement a secured party: but by virtue of its failure to register Bloodstock it never had priority over Lock.

[46] Section 109 of the PPSA as then in force provided:

> **Secured party may take possession of and sell collateral**
>
> (1) A secured party *with priority over all other secured parties* may take possession and sell collateral when –
>
> (a) The debtor is in default under the security agreement; or
>
> (b) The collateral is at risk.
>
> ...
>
> (Our emphasis.)

[47] Mr Black submits that s 109 as it then stood limited the right to take possession and sell Generous to Lock alone. He relies on *Jenkins* where

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[36] PPSA, s 16(1), definition of "security agreement".
[37] PPSA, s 17.
[38] PPSA, s 16(1), definition of "perfected by registration".

Winkelmann J held that, as between the financiers, Lock with a first ranking security interest was the only party entitled by s 109 to take possession of and sell Generous. Winkelmann J reasoned that:[39]

> [154] This provision [s 109] only gives a right of repossession and sale to the party with a first ranking security interest, in this case, in Generous. There has been significant and justified criticism of the limitation of the repossession right created by the inclusion of the words "with priority over all other secured parties". As the authors [Mike Gedye, Ronald C Cuming and Roderick J Wood] of [*Personal Property Securities in New Zealand* (Brookers, Wellington, 2002)] state, it will not always be obvious which secured party has priority over all others. Sometimes priority will have to be worked out through the Courts, because priority may not always be determined by reference simply to time of registration. ...
>
> [155] Whatever the difficulties with s 109, in this case [Bloodstock] was not "a secured party with priority over all other secured parties". Although s 109 is a provision that can be contracted out of, the parties did not do so; they expressly incorporated the rights available under the Act. [Bloodstock] therefore did not have a right to take possession of and sell Generous. In taking possession of Generous and in selling Generous, [Bloodstock] prima facie committed an unlawful act, namely conversion.

[48] In *Jenkins* Bloodstock was suing the guarantors of Glenmorgan's obligations. In the context of considering a right of counterclaim, Winkelmann J held that Bloodstock's possession of and sale of Generous was prima facie in breach of s 109. Its actions were unlawful as a result. The Judge's analysis was undertaken when evaluating the respective rights of Lock and Bloodstock. However, with respect, she proceeded on the erroneous factual premise that Bloodstock not only took possession of Generous but also sold him. As we have emphasised, it took only the former step.

[49] In *Jenkins* Winkelmann J endorsed academic criticism of the limitation on the right of taking possession and sale imposed by the words "with priority over all other secured parties" in s 109(1). That phrase has since been repealed with the effect that subordinate parties are also entitled to exercise the same right. We do not need to consider that question further here.

[50] That is because the PPSA allowed parties to contract out of its provisions.[40] In our judgment, bearing in mind the commercial purpose of the restructuring arrangement on 22 August 2003, cl 5(a) of the RA can be construed as the parties

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39 *New Zealand Bloodstock Leasing Ltd v Jenkins* (2007) 3 NZCCLR 811 (HC).

40 See the PPSA, s 107.

agreement to contract out of s 109 of the PPSA in so far as it may be construed as limiting the power to take possession to a first ranking secured party. By agreement, they were extending the same power to Bloodstock, whether as a first or subsequent ranking security holder.

[51] Winkelmann J's conclusion in *Jenkins* was not fatal to Bloodstock's claim against the guarantors. The Judge held that Glenmorgan would not have been able to recover any loss flowing from Bloodstock's unlawful act on these grounds:

> [165] I proceed to consider this issue as it raises a further, obvious and fundamental obstacle in the way of such a counterclaim. It is by reason of Glenmorgan's breach of contract in having granted a prior security interest that [Bloodstock] did not have the enforcement rights it had contracted for. If, as Glenmorgan had warranted and undertaken, Generous was free of prior ranking charges, the repossession would have been lawful. Any claim by Glenmorgan based on wrongful repossession would therefore fail on at least two bases.
>
> [166] Firstly, any claim for damages by Glenmorgan for damages for conversion could be met with a counterclaim by [Bloodstock] for breach of contract (clause 8 of CCA). Secondly, such a claim could be met with the plea that Glenmorgan cannot rely upon its own wrong (breach of contract) to found a claim: *New Zealand Shipping Company Ltd v Société des Ateliers et Chantiers de France* [1919] AC 1.

[52] While Potter J relied on these grounds also, Mr Morgan did not develop an argument in support of them. And we question whether they are sustainable. A right of counterclaim cannot operate to extinguish liability for the commission of a tort but goes to damages only; and it is questionable whether Glenmorgan's breach of contract – if it occurred – caused Bloodstock's loss of priority.

(e) Estoppel by conduct

[53] Before leaving this part of the judgment we refer to a submission by Mr Black. He says that Bloodstock is estopped by its conduct in the *Waller* and *Jenkins* proceedings from denying Glenmorgan's possessory interest. In *Waller*, he says, the financier relied upon LPA2 to justify its seizure of Generous; in *Jenkins* by contrast, it no longer relied upon LPA2 as it had been repaid and title with the corresponding right to possession had passed to Glenmorgan.

[54] The principle of estoppel by conduct in proceedings is settled.[41] A party's conduct in legal proceedings may estop it from adopting an inconsistent position in later proceedings. It may be unconscionable to allow a party which has secured the benefit of a finding in litigation from changing course because its interests have changed, especially where it is to the prejudice of the party which has acquiesced in the position formerly taken.

[55] However, it is unnecessary for us to address Mr Black's submission. We have already found that Glenmorgan had standing to bring its claim for conversion because it was lawfully in possession of Generous when Bloodstock seized him. Our inquiry has been into the nature and extent of Bloodstock's right.

(f) Conclusion

[56] Accordingly, we are satisfied that Bloodstock had a right conferred by cl 5(c) of the RA to take possession of Generous on 7 July 2004; and that that right was necessarily superior to Glenmorgan's concurrent right of possession. It follows that Bloodstock's action was justified.

[57] We add that normally we would have sought further submissions from counsel on a point which was not raised in argument (see our discussion at [39]–[44] above). However, we do not consider that course necessary, given our conclusion on causation and loss, which is to follow.

Loss

(a) Glenmorgan's claim

[58] This section of our reasons, addressing the second question of whether Glenmorgan suffered any loss, proceeds on an assumption (which we do not accept) that Bloodstock was not justified in taking possession of Generous on 7 July 2004. Potter J found briefly against Glenmorgan on this issue.

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[41] See K R Handley *Spencer Bower and Handley: Res Judicata* (4th Ed, Lexis Nexis, London, 2009) at [9.46].

[59] Glenmorgan claimed two heads of loss: first, for capital loss of $3.8 million being the market value of Generous when he was seized on 7 July 2004; and, second, for loss of profits for six years estimated at $3.6 million. Bloodstock countered that the stallion's value when seized was $1.013 million – the sale price realised a year later – and that Glenmorgan suffered no consequential loss.

[60] Experts were called to support the conflicting contentions advanced by the parties on value. Potter J did not consider it necessary to decide the valuation dispute. Instead she found that as a matter of fact Glenmorgan could not establish any loss.

[61] The facts relevant to Potter J's findings are:

(a) On 25 July 2004, within a few weeks of Bloodstock taking possession of Generous, Lock appointed receivers to Glenmorgan. Lock's notice dated 23 July relied on two defaults under its debenture – a failure to pay interest due of $104,062 and Bloodstock's taking possession of Generous.

(b) Glenmorgan's own defaults precipitated its receivership. Bloodstock's action in seizing Generous did not in itself cause the receivership. By early July 2004 Lock had already lost confidence in the company.

(c) Even though the financiers were in dispute over priority, Bloodstock and Lock cooperated in managing Generous which continued as before to generate income from service fees over the ensuing year.

(d) All income derived from Generous' activities was applied in reduction of Glenmorgan's indebtedness to Lock.

(e) Glenmorgan's receivers, not Bloodstock, sold Generous for $1.013 million dollars in June 2005.

(b) Principles

[62] Mr Black puts Glenmorgan's case for damages on an absolute premise. In his submission Glenmorgan must be entitled to an award to be measured by Generous' market value at the date of conversion. All its evidence was directed to that end. However, Mr Black's argument is, we think, misconceived.

[63] In the *Kuwait Airways* case Lord Nicholls examined the development of English law in the areas of causation and loss consequent upon liability for the tort of conversion. Claims had been made in that case for capital and consequential loss following the expropriation by armed force of commercial aircraft.[42] On the date for fixing damages, Lord Nicholls said this:

> 67 ... The aim of the law, in respect of the wrongful interference with goods, is to provide a just remedy. Despite its proprietary base, this tort does not stand apart and command awards of damages measured by some special and artificial standard of its own. The fundamental object of an award of damages in respect of this tort, as with all wrongs, is to award just compensation for loss suffered. Normally ("prima facie") the measure of damages is the market value of the goods at the time the defendant expropriated them. This is the general rule, because generally this measure represents the amount of the basic loss suffered by the plaintiff owner. He has been dispossessed of his goods by the defendant. Depending on the circumstances some other measure, yielding a higher or lower amount, may be appropriate. The plaintiff may have suffered additional damage consequential on the loss of his goods. Or the goods may have been returned.

[64] Lord Nicholls recognised that the normal rule for assessing damages is general, not immutable. It must always yield to the overriding requirement that damages are designed to compensate in monetary terms for loss actually suffered. As *The Law of Torts in New Zealand* states:[43]

> The principle that the normal measure of damages in conversion is the market value of the goods [at the date of conversion] is consistent with the idea that the plaintiff is effectively forced to sell the goods to the defendant by virtue of the conversion. The judgment for the plaintiff, once satisfied, divests the plaintiff of his or her title to the goods and vests it in the defendant, the defendant being obliged to pay the value of the goods.

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42 *Kuwait Airways Corporation v Iraqi AirwaysCo (Nos 4 & 5)* [2002] UKHL 19, [2002] 2 AC 883 at [60] onwards.

43 Stephen Todd (ed) *The Law of Torts in New Zealand* (5th ed, Brookers, Wellington 2009 [12.3.04].

(Footnotes omitted.)

[65] In the *Kuwait Airways* case Lord Nicholls gave the return of an asset to its owner as a specific example of a case where a date other than the date of wrongful taking of possession is appropriate for measuring damages. That is because the plaintiff is not permanently deprived of ownership; there is no forced sale of its asset.

[66] The rule's flexibility is reflected in decisions of high authority. In *BBMB Finance* Lord Templeman referred to its general purpose as being to compensate a plaintiff "... whose property is irreversibly converted".[44] In *Brandeis Goldschmidt,*[45] a decision cited with approval by Lord Nicholls in the *Kuwait Airways* case,[46] Brandon LJ rejected the notion of a universally applicable rule for assessing damages for wrongful detention of goods, noting that the measure "... may vary infinitely according to the individual circumstances of any particular case".[47]

(c) Date for measuring loss

(i) Capital loss

[67] Is 7 July 2004 the correct date for assessing any loss suffered by Glenmorgan?

[68] Glenmorgan's primary claim is for the capital loss of $3.8 million, being the then market value of Generous, allegedly caused by Bloodstock's taking of the stallion's possession.. However, Glenmorgan's own case undermines its claim. The company did not intend to sell Generous in July 2004. Mr Black emphasises that the stallion was Glenmorgan's principal income earning asset. All the evidence points to its desire to retain ownership. That intention was not affected by Bloodstock's act of taking possession.

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44 See *BBMB Finance (Hong Kong) Ltd v EDA Holdings Ltd* [1990] 1 WLR 409 (PC).
45 *Brandeis Goldschmidt & Co Ltd v Western Transport Ltd* [1981] QB 864 (CA).
46 At [65].
47 At 870.

[69] The effect of any conversion by Bloodstock was not irreversible. Glenmorgan's proprietary right – its title to the stallion – remained undiminished. The asset was not alienated from Glenmorgan's ownership. And the company was not forced to buy a replacement. Moreover, within a few weeks of Generous' seizure, Lock appointed receivers of Glenmorgan. In law the receivers were Glenmorgan's agents.[48] On a date unknown but before selling Generous in June 2005 the receivers recovered possession of him.

[70] It would be artificial to treat 7 July 2004 as the date for fixing any damages because that would reward Glenmorgan for a purely notional loss. Bloodstock was at most responsible for a temporary interference with Glenmorgan's possession of Generous. Its right to damages would be limited to losses flowing from that finite period of deprivation.

[71] However, Bloodstock's interference did not cause Glenmorgan to lose its title to the horse. Nor was Glenmorgan forced to sell as a result of Bloodstock's taking of possession: its loss of possession did not equate to a loss of ownership. Mr Black relies on Bloodstock's allocation of a credit of $1.1 million against Glenmorgan's liability in September 2004 as evidence of its appropriation of Generous at that figure. But an internal accounting entry cannot amount of itself to evidence of an appropriation of title. Glenmorgan ultimately lost ownership of Generous as a result of its receivers' decision to sell Generous in June 2005. In the absence of a challenge to the receivers' authority to sell, the company must be taken to accept that its agents sold the stallion for the best price then reasonably obtainable.[49]

(ii) Loss of profits

[72] Glenmorgan's claim for lost profits is also unsustainable. The financiers co-operated in his management and in arranging service fees after Generous was seized. All income was lawfully paid to and applied by the receivers in reduction of Glenmorgan's indebtedness. The receivers were, we repeat, the company's agents.

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[48] See the Receiverships Act 1993, s 6(3).
[49] See the Receiverships Act 1993, s 19.

[73] The receivership occurred 18 days after Bloodstock took possession of Generous. Any loss of income in the intervening period would have been minimal. In apparent recognition of this fact, Glenmorgan's expert, Dennis Lane, calculated Glenmorgan's loss of profits from the date of the receivership's commencement. And Glenmorgan has not established that the stallion's income earning capacity was diminished while he was in Bloodstock's possession.

(d) Loss inevitable

[74] Alternatively, Glenmorgan's claim must fail on the ground that, even if it suffered loss, the loss was not caused by Bloodstock.

[75] In the *Kuwait Airways* case Lord Nicholls considered the relevant principles of causation when predicating this two stage enquiry: first, did the wrongful conduct causally contribute to the loss and, second, if it did, what is the extent of loss for which the defendant ought to be held liable?[50] While conversion is a tort of strict liability, orthodox principles of causation apply – a causal connection between breach and loss is necessary; the wrongful conduct must have been a substantial or proximate cause of loss; and questions of mitigation and remoteness may be relevant.[51]

[76] Lord Nicholls allowed that at the first stage there was room for a modified "but for" test, expressed in this way:

> 72 ... This guideline principle is concerned to identify and exclude losses lacking a causal connection with the wrongful conduct. Expressed in its simplest form, the principle poses the question whether the plaintiff would have suffered the loss without ("but for") the defendant's wrongdoing. If he would not, the wrongful conduct was *a* cause of the loss. If the loss would have arisen even without the defendant's wrong doing, normally it does not give rise to legal liability ...

[77] We need to go no further than the first of Lord Nicholls' two stages. There were two decisive inevitabilities facing Glenmorgan. The first was, on Potter J's findings, that Glenmorgan would fail in early July 2004. It was then in substantial

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50 At [69].
51 At [70].

default of its repayment obligations to both financiers, for which it alone was responsible; Potter J acquitted Bloodstock of any contributing blame. Lock appointed receivers of Glenmorgan in late July, relying both on Bloodstock's action and Glenmorgan's failure to pay a substantial interest instalment.

[78] The second inevitability was that, once Glenmorgan was placed in receivership, the receivers would sell its primary assets. The sale of Generous was a foregone conclusion. In causation terms, Bloodstock's action, while denying Glenmorgan's right of possession, was not an operative factor in either its loss of ownership or of the right to receive income from the stallion's activities prior to that. Those events would have happened regardless of Bloodstock's intervention.

(e) Failure to prove loss

[79] Alternatively, even if the date on which Bloodstock took possession of Generous was the correct date for measuring loss, we are not satisfied that Glenmorgan discharged its onus of proving its claim for lost capital or lost profits. As noted, Potter J did not consider it necessary to resolve the differences between the competing experts about Generous' value as at July 2004. However, having reviewed the transcript for ourselves, we agree with Mr Morgan that Glenmorgan's evidence led in support of its claim was unsatisfactory and failed to establish either a capital loss or lost profits.

(f) Conclusion

[80] In our judgment, even if it was unlawful, Bloodstock's taking of possession of Generous on 7 July 2004 did not cause Glenmorgan any loss.

Result

[81] Glenmorgan's appeal is dismissed.

[82] Glenmorgan is to pay Bloodstock costs for a complex appeal on a band A basis with usual disbursements. We certify for two counsel.

Solicitors:
Craig Griffin & Lord, Auckland for the Appellant
J G Collinge, Auckland for the Respondent