**IN THE COURT OF APPEAL OF NEW ZEALAND**

**CA698/2007**
**[2009] NZCA 122**

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|---|---|
| BETWEEN | J S BROOKSBANK AND COMPANY (AUSTRALASIA) LIMITED<br>Appellant |
| AND | EXFTX LIMITED (IN RECEIVERSHIP AND LIQUIDATION) FORMERLY KNOWN AS FELTEX CARPETS LTD<br>First Respondent |
| AND | COLIN NICOL & OTHERS<br>Second Respondents |

Hearing: 4 November 2008

Court: William Young P, O'Regan and Arnold JJ

Counsel: G H J Brant and R J T Robertson for Appellant
L A O'Gorman and S R Willetts for First and Second Respondents

Judgment: 6 April 2009 at 2.30 pm

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**JUDGMENT OF THE COURT**

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**A The appeal is allowed.**

**B The respondents must pay the appellant costs for a standard appeal on a band A basis, plus usual disbursements. We certify for two counsel.**

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**REASONS OF THE COURT**

(Given by Arnold J)

## Introduction

[1] The appellant, JS Brooksbank & Co (Australasia) Limited (JSB), supplied wool to Feltex Carpets Limited. The latter company went into receivership in September 2006 and is now known as EXFTX Limited (in receivership and liquidation), the first respondent. We will simply refer to it as Feltex. The second respondents, principals in the firm of McGrathNicol+Partners, are Feltex's receivers.

[2] JSB supplied wool to Feltex for its Kakariki wool scour under a short-term supply contract. When Feltex went into receivership, certain wool mistakenly supplied by brokers on behalf of JSB and not paid for by Feltex was on Feltex's premises. The receivers took control of it. JSB sued in conversion to recover it. Feltex and the receivers said that JSB's interest in the wool was an unperfected security interest under the Personal Property Securities Act 1999 (PPSA) which did not take priority over the perfected security interest of ANZ National Bank Limited and Australia and New Zealand Banking Group Limited (ANZ), which had a composite debenture with Feltex. The debenture had been registered on the Personal Property Securities Register (the register).

[3] Stevens J held that JSB's claims in conversion and constructive trust could not succeed and that JSB had an unperfected security interest over which ANZ's perfected security interest took priority: HC AK CIV 2006-404-5963 21 November 2007. JSB appeals from that decision.

## Factual background

[4] ANZ was a major lender to Feltex. It had entered into a composite debenture with Feltex in May 2000, creating a charge over all present and after acquired property. ANZ registered financing statements on the register in relation to the debenture in 2002 and 2006 and in PPSA terms had a perfected security interest in present and after-acquired property of Feltex.

[5] JSB had been supplying wool to Feltex for some time but needed to establish new supply arrangements when its insurers withdrew credit cover in respect of its

dealings with Feltex on 30 June 2006. This occurred because Feltex was known to be undergoing financial difficulties at the time. Accordingly, on 22 August 2006 JSB and Feltex entered into a written contract for the supply of wool (the supply agreement) for the period 1 August to 31 October 2006. JSB was to supply wool for Feltex's Kakariki scour (situated in Halcombe, Manawatu) on a monthly basis in specified quantities, with the price to be established and advised each month according to a formula.

[6] The effect of the supply agreement was that Feltex would obtain neither possession of, nor title to, any wool until after JSB had received payment by way of cleared funds. Once JSB had received cleared funds, title to the relevant wool passed immediately to Feltex, even although JSB still had possession. So title passed before delivery, rather than the other way round (as is typical in contracts containing retention of title clauses). These points are clear from the following provisions:

> **4.0 TERMS OF SUPPLY**
>
> The contract shall be based on:
>
> …
>
> - Payment will be made on a cash on delivery basis following presentation of documents.
>
>  1. [JSB] are to supply a Certificate to confirm the following:
>
>  Upon receipt of notification of cleared funds, unconditional ownership of the wool passes to the purchaser, [Feltex]. This arrangement includes any wool held by the seller.
>
>  2. The Feltex (sic) will advise the seller (JSB) when payment is made. Feltex agrees that cleared funds will be advised prior to the despatch of the wool.
>
>  3. JSB will arrange to pay for the applicable insurance costs incurred in meeting the above requirements. Feltex will invoice these costs directly.
>
> - The scour is to be advised of the wool storage location no later then seven days prior to the contracted delivery date.
>
> …

**7.0 GENERAL**

…

6. Price Basis

   All wools to be purchased on the following basis

   …

   - Payment: ~~Cash on delivery and presentation of documents~~. Delivery made on reciept [sic] of cleared Bank funds.

   …

8. Delivery to be made by the 5th day of each month.

[7] The amendment to the struck out portion of the payment clause was in handwriting, and was made by JSB's chief executive. There is no dispute that it was the agreed position. Plainly, the reason for making delivery conditional on the receipt of cleared funds was to protect JSB's position.

[8] Under the supply arrangements, when JSB received cleared funds from Feltex, it was to notify Feltex (by way of a certificate – see point 1 in cl 4 at [6] above). This reflected the fact that ANZ would transfer the funds to JSB's account as "same day cleared funds" (ANZ was also JSB's banker), and Feltex would receive notification of the funds transfers the day after they were made. When JSB received payment it would send a buyer delivery order (BDO) to the wool stores holding the relevant wool. The BDOs authorised the wool stores to release the wool to Feltex's carriers.

[9] Between 25 and 30 August 2006, JSB issued four invoices to Feltex for wool ordered for the September requirements at the scour. Each of the invoices was marked as followed:

> WOOLS WILL BE RELEASE [sic] TO YOUR ORDER UPON RECEIPT OF PAYMENTS RECEIVED IN OUR ACCOUNT

[10] These invoices related to several different lots of wool held at various wool stores around the country. Ms South, Feltex's financial controller who worked at Feltex's office in Foxton, submitted a bill funding note to ANZ in respect of the

wool ordered for September delivery, with a request that payment be made on 4 September 2006.

[11] According to Mr Berry, Feltex's wool buying manager who worked at the Kakariki scour, the normal practice was that he would check a list of invoices daily to see which had been paid. Where invoices had been paid, Mr Berry would authorise staff to order in the relevant wool. Ms South disputed that, however. She said that JSB had the obligation of satisfying itself that cleared funds had been received before releasing the wool. From the perspective of the scour, the process remained as it had previously, with wool being called in on the specified payment date for release the following day.

[12] Whatever the true position, the system broke down in relation to the wool at issue. At the beginning of September 2006, Ms Gust had returned to work at the scour, having been on maternity leave since February 2006. Part of her employment responsibilities were ordering and arranging transport for wool to the scour. She was advised of the supply agreement in a quick "catch up" conversation. Although she was told that JSB required confirmation of payment before it would release any wool, she was not told that the payment for the September wool had not yet been made.

[13] On Monday 4 September, her first official day back at work, Ms Gust found on her desk a set of orders for JSB marked "Pick up for Tuesday". She assumed that payment had been made, and despatched facsimiles to each of the relevant wool stores seeking release of the wool to Feltex's carriers.

[14] Late in the afternoon of 4 September some brokers contacted Ms Gust to say that, as they had not received BDOs from JSB, they would not be releasing the wool. Other brokers contacted JSB to ask whether they could release the wool even though they had not received BDOs. JSB advised that they should not release the wool. However, some brokers did release wool to Feltex's carriers when they turned up on 5 September, even though they had not received BDOs. The unpaid price for this wool was $132,839.11 (including GST), and it is this that is the subject of the present dispute.

[15] Also on 5 September Ms South received a bank statement from ANZ which showed that ANZ had not transferred funds to JSB in payment for the wool the previous day. She attempted to contact ANZ to find out what the position was. Feltex resubmitted the bill funding notice to ANZ everyday thereafter, until the receivers were appointed on 22 September.

[16] On or about 12 September Mr Berry learned that Feltex had received the wool without having paid for it. He arranged to have the wool put to one side and not scoured. After the receivers had been appointed, one of their employees, Mr Barrett, visited the scour. Mr Berry told him about the wool and said that Feltex could not use it as it had not been paid for and should not have been in Feltex's possession. However, the receivers did not agree. They considered that Feltex was legally entitled to use the wool and was under no obligation to return it to JSB. Apparently, JSB first learnt that Feltex had the wool around 26 September, when the receivers advised them of it.

[17] JSB immediately sought return of the wool. The receivers refused to return it. On 29 September JSB issued proceedings, and applied for an ex parte interim injunction restraining Feltex and the receivers from disposing of or using the wool. This application was withdrawn when the receivers gave an undertaking to abide by whatever order the Court might make as to damages.

**Basis of appeal**

[18] In the High Court, Stevens J found:

(a) **No conversion**: Feltex did not convert the wool because JSB, through its agents, had voluntarily delivered it: at [66] – [69]. The Judge relied in particular on *Jeffcott v Andrew Motors Limited* [1960] NZLR 721 (CA), *PGG Wrightson Limited v Wai Shing Limited* HC AK CIV 2003-404-6579 25 August 2006 and *Dennant v Skinner & Collom* [1948] 2 KB 164.

(b) **No constructive trust**: The imposition of a constructive trust was not justified, as there was no unconscionable conduct by Feltex: at [71] – [74].

(c) **PPSA applied**: JSB's interest in the wool following its delivery to Feltex amounted to a security interest for the purposes of the PPSA. In terms of s 17(1)(a), the supply agreement was a conditional sale contract. It was an agreement to sell subject to a retention of title provision (i.e. cl 4 of the supply agreement): at [52]. The Judge said that when the brokers released the wool to Feltex's carriers, Feltex obtained possession of it and, in accordance with s 40, having acquired rights in the wool, the security interest had attached: at [56] – [57]. The perfected interest of ANZ had priority over the unperfected interest of JSB under the provisions of the PPSA: at [76].

[19] In this Court, Mr Brant for the appellant challenged each of these findings.

**Discussion**

[20] Adopting the parties' approach, we will deal first with conversion and then move on to the PPSA arguments.

*Conversion*

[21] The ingredients of the tort of conversion are discussed in *Kuwait Airways Corporation v Iraqi Airways Co (Nos 4 and 5)* [2002] 2 AC 883 (HL(E)). Lord Nicholls of Birkenhead said (at [39]):

> 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.

[22] Later, Lord Nichols said (at [42]):

> [M]ere unauthorised retention of another's goods is not conversion of them. Mere possession of another's goods without title is not necessarily inconsistent with the rights of the owner. To constitute conversion detention must be adverse to the owner, excluding him from the goods. It must be accompanied by an intention to keep the goods.

[23] In the present case Stevens J held that Feltex did not convert the wool because JSB, through the brokers, released it voluntarily. (It was common ground that the brokers were JSB's agents.) Mr Brant submitted that the Judge was wrong to make this finding. The effect of his argument was that the brokers who released the wool had express authority to do so only after receipt of a BDO from JSB. Having received no relevant BDO, they were not acting within the scope of their express authority. Accordingly, the issue was whether they had either implied or apparent authority. Implied authority may arise as a necessary term of the agreement between the parties, or from trade custom or usual practice. In the present case the brokers did not have implied authority to release wool without receiving a BDO as that would have been inconsistent with the terms of their express authority. Nor was there any evidence that the brokers had authority to waive the contractual requirements on behalf of JSB. So the question was whether they had apparent authority.

[24] As to that, Mr Brant relied on the decision of this Court in *Savill v Chase Holdings (Wellington) Limited* [1989] 1 NZLR 257 to argue that only a principal's representation that an agent has authority can clothe an agent with apparent authority. He argued that there was no such representation in the present case. The parties were, he said, attempting to perform the contract in accordance with its terms. When Mr Berry realised that the wool had not been paid for, he immediately put it to one side and later advised the receivers that it should not be in Feltex's possession. When JSB learnt that Feltex had the wool towards the end of September 2006, it immediately sought its return.

[25] Ms O'Gorman for the respondents argued that when the wool was released to Feltex's carriers, there was nothing to indicate that the brokers were acting outside the terms of their express or implied authority. Feltex took possession of the wool believing that JSB's agents had acted within the scope of their authority. The agents did exactly what they were authorised to do, namely, give possession of the wool.

Ms Gorman relied in particular on the three authorities referred to at [18](a) above. She submitted therefore that the real issue concerned the statutory consequences of delivery under the Sale of Goods Act 1908 and the PPSA. Accordingly, through its brokers, JSB voluntarily released the wool, with the consequence that an action in conversion could not succeed.

[26] We agree with Mr Brant's analysis, first because we consider that agency principles mean that the delivery was not "voluntary" as between JSB and Feltex and second, because we consider that the authorities relied on by Ms O'Gorman and accepted by the Judge are distinguishable.

[27] Dealing first with agency, the basic principle is set out in *Bowstead & Reynolds on Agency* (18ed 2006) as follows (at [8-160]):

> Subject to [certain qualifications], where an agent disposes of the property or money of his principal in a manner not authorised, ratified or otherwise valid, the principal is entitled, as against the agent and third parties, to recover that property or money, or the proceeds of that property or money, wherever they may be found, provided that they can be traced in accordance with the rules of common law and equity.
>
> (Footnote omitted.)

As the authors note, the primary means of achieving this is through an action in conversion: at [8-161].

[28] It was not disputed that the brokers did not have express authority from JSB to release the wool prior to receipt of a BDO. Their express authority simply reflected the arrangements set out in the supply agreement. Further, we do not see how it can sensibly be suggested that they had implied authority to do so, as that would have been inconsistent with their express authority. So the issue is one of apparent (or ostensible) authority.

[29] In our view, there are two difficulties with saying that the brokers had apparent authority.

[30] First, as Mr Brant said, the existence of apparent authority depends on there being a representation by the principal, JSB. The principal is treated as being

estopped from denying the agent's authority. A representation by the agent is accordingly not of itself sufficient. See the discussion in *Savill* at 304 – 305. There has been no suggestion that JSB represented, whether specifically or by its conduct, that its agents had authority to release wool prior to the receipt of cleared funds. Nor do we see how it can be said that JSB acquiesced in the release on this occasion, as it did not know about it and, when it found out, it immediately demanded the wool's return. Accordingly, we do not consider that JSB was estopped from denying that the brokers had authority to release the wool.

[31] Second, apparent authority cannot arise given that Feltex knew that the brokers were authorised to release wool only after cleared funds had been received. In *Armagas Limited v Mundogas SA* [1986] AC 717 (HL(E)) at 777 Lord Keith of Kinkel emphasised that apparent authority cannot arise where a party such as Feltex "knows that the agent's authority is limited so as to exclude entering into transactions of the type in question". Feltex was not under any misapprehension as to the limits of the brokers' authority. Rather, Feltex's Ms Gust thought that payment had been made, so that Feltex was entitled to call for release of the wool. In other words, from Ms Gust's perspective, the brokers were acting within the terms of their express authority. But others within the Feltex organisation were aware that payment had not been made, in particular Ms South. In any event, none of the relevant Feltex personnel believed that the brokers were entitled to deliver wool before payment by way of cleared funds had been made.

[32] We turn now to the three authorities relied upon by Ms O'Gorman. To reiterate, she submitted that when JSB's agents allowed Feltex's carriers to uplift the wool, they had done precisely what they were authorised to do – to give possession. She submitted that Feltex had no knowledge that JSB's agents had breached the terms of their agency in releasing the wool. It was in this context that she relied on the authorities.

[33] We begin with *Jeffcoat v Andrew Motors Ltd*. In that case a fraudster purchased a car from its owners (a married couple) by means of a worthless cheque and then sold it to a car dealer. The owners sued the car dealer for the return of the car or for damages. They were unsuccessful.

[34] It was undisputed that that property in the car passed to the fraudster. This Court held that the car dealer obtained good title to the car by virtue of ss 25 and 27(2) of the Sale of Goods Act. Under s 27(2) the sale from the fraudster to the car dealer was to have "the same effect as if the person making the delivery or transfer were a mercantile agent in possession of the goods or documents of title with the consent of the owner". One of the arguments raised by the owners was that the fraudster had dealt with the wife, so that while he may have obtained possession of the car with her consent (albeit based on a mistake as to the worth of the cheque), he did not have the consent of the husband. The Court rejected that argument. The husband had authorised the wife to sell the vehicle. In exchanging the vehicle for the cheque she did not contravene her husband's instructions. Despite the deceit, her consent was real and that must bind the husband as well: per Gresson P and Cleary J at 729. So the fraudster, having obtained possession of the car with the consent of the couple, was able to effect a transfer to Andrews Motors Ltd which was a bona fide purchaser for value without notice.

[35] We do not see that case as assisting in the present context. It was clear that the wife was authorised to sell the car and to accept a cheque. The couple did not apparently contemplate the possibility that the cheque would not be honoured. The Court said that the husband would have been treated as having consented had the cheque been honoured, and the same must apply where the cheque was dishonoured. In the present case, the question of non-payment was specifically addressed, in the sense that the brokers were forbidden to release the wool until they had received BDOs following the receipt of cleared funds. They acted contrary to their specific instructions. Ms O'Gorman argued that Feltex was not aware of that. But Feltex knew that the wool was not to be released until payment. That was the whole point of the supply agreement. While Feltex may not have known all the detail of JSB's arrangements with its agents, it undoubtedly knew that they could not release wool prior to the receipt of cleared funds. Indeed, its mistake (through Ms Gust) was not about the scope of the brokers' authority – rather, it was about whether payment had been made. In our view, JSB did not consent to release in those circumstances.

[36] *Dennant v Skinner & Collom* was a case with similar facts. An auctioneer (the plaintiff) knocked a car down at auction to a fraudster, who paid him with a

cheque that was dishonoured. The car was on-sold to a person who had no notice of the fraud (the subsequent purchaser). The auctioneer sued the subsequent purchaser for the return of the car or its value. The Court held that the property in the car had passed to the fraudster on the fall of the hammer, but the auctioneer had the right under the Sale of Goods Act 1893 to retain possession until payment was made. However, he had parted with possession of the car by giving delivery, and so lost his seller's lien and the right to possession: at 172. Accordingly he failed in his action.

[37] Again, we do not see this case as providing assistance. As in *Jeffcoat v Andrews Motors Ltd*, property had passed to the fraudster and possession was given on the basis of a mistake about the worth of a cheque tendered in payment. In the present case, property in the wool had not passed, and the agents acted outside the express limitations on their authority when releasing the wool, limitations of which Feltex was aware (in the sense that it knew that wool could not be released prior to the receipt of cleared funds).

[38] Finally we come to *PGG Wrightson Limited v Wai Shing Limited*. Fruitfed was a wholesaler of fruit and vegetables. It operated through a number of outlets, which had their own managers. They had some flexibility as to the prices they charged, to reflect local market conditions. One manager sold produce at prices below those that Fruitfed would have authorised. When it discovered what the manager had done, Fruitfed did not repudiate the contracts but sued the purchasers for the shortfall between what that it said the purchasers should have paid for the produce and what in fact they paid. Among the causes of action was one in conversion.

[39] Keane J dismissed the conversion claim, on the ground that voluntary delivery displaces conversion, even when induced by fraud: at [56].

[40] However, the Judge said:

> [54] … [The manager] was Fruitfed's branch manager with ostensible authority to commit Fruitfed on price and terms in the highly competitive Pukekohe market and only Fruitfed knew what the scope of his actual authority was. Fruitfed must therefore carry the ultimate persuasive onus of

> showing that [the purchasers] must have been aware that, whatever [the manager's] actual authority was he surely exceeded it.

[41] That, of course, was not the position in the present case. As we have said, Feltex knew that wool was not to be released prior to the receipt of cleared funds. Ms Gust's mistake was not about the scope of the agents' authority but about whether payment had been made.

[42] Stevens J said that the delivery of the wool created a debt which Feltex was obliged to meet: at [51]. However, we consider that Feltex was not obliged to accept delivery, and could simply have returned the wool, as Mr Berry contemplated. For its part, JSB was entitled to seek the return of the wool. We return to this point at [56] below.

[43] We now turn to the effect of the PPSA.

*The PPSA and its application in this case*

[44] The PPSA introduced a new approach to rights in personal property falling within its scope. The background to it is outlined in this Court's decision in *Waller v New Zealand Bloodstock Ltd* [2006] 3 NZLR 629, especially at [12] – [14]. There the Court said:

> [13] The key features of our PPSA … are the adoption of a unitary concept of security (under which the legal forms by which security is obtained become largely irrelevant) and establishment of priority rules which depend primarily on time of registration save for the super-priority accorded to registered purchase money security interests (that is, in favour of unpaid vendors) over prior general securities.

See also William Young J's dissenting judgment at [89] – [91]. In an observation pertinent to the present case, the Judge said that the PPSA "equates what the law previously regarded as true security interests (for example, created by a chattel mortgage) and in substance security interests (for example, pursuant to a *Romalpa* clause)": at [89].

[45] The concept of "security interest" is central to the PPSA. It is relevantly defined as follows:

> **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
>
> …
>
> (3) Without limiting subsection (1), and to avoid doubt, this Act applies to a fixed charge, floating charge, chattel mortgage, conditional sale agreement (including an agreement to sell subject to retention of title), hire purchase agreement, pledge, security trust deed, trust receipt, consignment, lease, an assignment, or a flawed asset arrangement, that secures payment or performance of an obligation.

[46] As the Judge said (at [37] – [40]), under the PPSA retention of title is not the determinative factor. The fact that a secured party (that is, a person holding a "security interest") holds title is not critical in terms of the PPSA's operation: see ss 17 and 24.

[47] A security interest may be perfected or unperfected. These terms are defined in s 16. A perfected security interest means that the security interest is "perfected by possession or by registration or is temporarily perfected, as the case may be". An unperfected security interest means a security interest that is not a perfected security interest. In the present case, there is no dispute that the ANZ debenture was a perfected security interest, and that, if JSB had a security interest, it was unperfected.

[48] Section 40 deals with the attachment of security interests to collateral. That section relevantly provides:

> **40 Attachment of security interests generally**
>
> (1) A security interest attaches to collateral when–
>
> (a) Value is given by the secured party; and
>
> (b) The debtor has rights in the collateral; and

> (c) Except for the purpose of enforcing rights between the parties to the security agreement, the security agreement is enforceable against third parties within the meaning of section 36.
>
> …
>
> (3) For the purposes of subsection (1)(b), a debtor has rights in goods that are leased to the debtor, consigned to the debtor, or sold to the debtor under a conditional sale agreement (including an agreement to sell subject to retention of title) no later than when the debtor obtains possession of the goods.
>
> ….

[49] Turning to the present case, the first question is whether the supply agreement created a security interest in terms of s 17. Specifically, the question is whether JSB had an interest in personal property (the wool) provided for by a transaction (the supply agreement) that in substance secured payment, ignoring the form of the transaction and the fact that JSB retained title.

[50] It seems clear that the supply agreement was not intended to secure payment in the manner contemplated by the definition. Rather, the basis of the supply agreement was that Feltex could not take delivery until it had received notification from JSB that JSB had received cleared funds, by which time title would already have passed to Feltex. Clause 4 of the supply agreement was not a retention of title clause as that term is generally understood. Retention of title clauses commonly appear in contracts which contemplate the possibility of delivery of goods prior to payment and are intended to enable the supplier to have recourse to the goods if payment is not made subsequently.

[51] Here delivery prior to JSB receiving cleared finds and notifying Feltex has occurred by error. While the result is that Feltex obtained possession and JSB retained title, that combination of circumstances was not something contemplated by the supply agreement. It seems to us difficult to say that the supply agreement "in substance" secured payment when it was based on a wholly different premise, namely that there could be no delivery until payment had been made. The direction to have regard to what a transaction does "in substance" suggests that the focus

should be on "what the transaction purports to do": Widdup & Mayne *Personal Property Securities Act: A conceptual approach* (2002) at [2.9].

[52] Unlike the typical retention of title situation, the supply agreement did not purport to enable JSB to have recourse to wool if payment was not made, that is, it did not purport to create or recognise a proprietary interest in favour of JSB in wool in Feltex's possession. Rather, it was intended to prevent any such issue from arising. In that sense, if there was a security interest in the present case, it arose accidentally. Looking at the matter from Feltex's perspective, it did not by means of the supply agreement purport to create or recognise a security interest in wool in its possession by recognising or granting rights in relation to it to JSB. Again, that situation was not contemplated by the supply agreement.

[53] Section 17(3) provides that the Act applies to a conditional sale agreement including an agreement to sell subject to retention of title. As we have said, the Judge concluded that the supply agreement was such an agreement and it was this that led him to find that there was a security interest. However, the specific arrangements referred to in s 17(3) will only qualify as security interests if they secure payment or performance of an obligation. This is clear from the final words of s 17(3). This language takes us back to the core concept in s 17(1), and to the point just discussed. For our part, we do not consider that cl 4 purports to be a retention of title clause as that term is generally understood. Unlike the Judge (at [55]), we consider that this distinguishes the present case from *Segard Masurel (NZ) Limited v Nicol* (2008) 10 NZCLC 264,386 (HC), which also arose out of the Feltex receivership but which, on the facts assumed by the Judge for the purposes of his PPSA analysis, concerned a true retention of title clause.

[54] Accordingly, we do not consider that the supply agreement gave rise to a transaction that "in substance" secured payment by Feltex. The supply agreement was specifically formulated to prevent JSB from having any credit exposure to Feltex. The fact that on this particular occasion, delivery was mistakenly effected prior to payment but title did not transfer does not change an arrangement that did not in substance create a security interest into one that did.

[55] Looking at the matter from ANZ's perspective, it clearly had a security interest. But, in our view, its security interest had not attached to the wool. Under s 40(1) a security interest attaches to collateral when, among other things, the debtor has rights in the collateral. Section 40(3) provides that a debtor has rights in goods sold under a conditional sale agreement (including an agreement to sell subject to retention of title) no later than when the debtor obtains possession of the goods. Here, however, the goods were not "sold" under the supply agreement and Feltex had no right of possession as against JSB.

[56] It follows from the foregoing analysis that we do not agree with the Judge that once the wool was delivered, Feltex had an obligation to pay for it: at [51]. The supply agreement did not provide for possession to be given prior to title passing. When Feltex obtained possession of the wool prior to obtaining title by making payment, it did not, in our view, have any rights in the wool or any obligation to pay for it. The wool was not delivered in accordance with, or appropriated to, the supply agreement. Feltex could not utilise the wool but was obliged to return it, as Mr Berry recognised.

*Conclusion*

[57] In the result, then, we consider that:

(a) JSB is entitled to sue in conversion for the return of the wool as it was not a volunteer;

(b) The position is not affected by the PPSA as JSB did not have a security interest and ANZ's security interest had not attached to the wool.

In view of these findings we need not address the constructive trust argument.

## Decision

[58] The appeal is allowed. The respondents must pay the appellant costs on a band A basis for a standard appeal, plus usual disbursements.

Solicitors:
Stace Hammond, Hamilton for Appellant
Buddle Findlay, Auckland for First and Second Respondents