

**IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY**

CIV 2006-404-5963

BETWEEN JS BROOKSBANK & CO
(AUSTRALASIA) LIMITED
Plaintiff

AND EXFTX LIMITED (IN RECEIVERSHIP
AND LIQUIDATION) FORMERLY
KNOWN AS FELTEX CARPETS
LIMITED
First Defendant

AND COLIN NICOL & OTHERS
Second Defendants

Hearing: 14 May and 8 November 2007

Appearances: G Brant and R Robertson for the plaintiff
L O'Gorman and S Willets for the defendants

Judgment: 21 November 2007

JUDGMENT OF STEVENS J

*This judgment was delivered by me on Wednesday, 21 November 2007 at 4pm
pursuant to r 540(4) of the High Court Rules.*

Registrar/Deputy Registrar

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JS BROOKSBANK & CO (AUSTRALASIA) LTD V EXFTX LTD (IN RECEIVERSHIP & LIQUIDATION)
FORMERLY KNOWN AS FELTEX CARPETS LTD And Anor HC AK CIV 2006-404-5963 [21 November
2007]

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Introduction

[1] In September 2006, Feltex Carpets Ltd went into receivership. Shortly before this, the Kakariki wool scour operated by Feltex required additional supplies of wool for that month. Wool was sourced from various brokers in different parts of the country pursuant to a commercial agreement between Feltex and the plaintiff, JS Brooksbank & Co (Australasia) Ltd (JSB), one of Feltex's wool suppliers. This case concerns a claim for conversion of the wool so obtained by Feltex. The first defendant is EXFTX Ltd (in receivership and in liquidation), the entity formerly known as Feltex. The second defendants are Feltex's receivers. A key factual question concerns the circumstances in which the wool came into Feltex's possession.

[2] Also at issue is the effect, if any, of the provisions of the Personal Property Securities Act 1999 (the PPSA). Feltex and the receivers contend that JSB's interest in the wool simply amounted to an unperfected security interest under the PPSA, which did not take priority over the perfected security interest of the ANZ National Bank Ltd (ANZ). That perfected security interest arose pursuant to a composite debenture that had been registered on the Personal Property Securities Register (PPSR). JSB says that the terms of the supply contract make it clear that Feltex was

not entitled to possession of the wool and hence converted it. Moreover, JSB had no security interest in the wool that came within the provisions of the PPSA.

[3] The case began as an application for an interim injunction by JSB against the receivers. Shortly after the proceeding was filed, the receivers provided an undertaking as to damages and agreed to abide any decision of the Court on questions of liability. The parties are agreed that the quantum of the JSB claim is \$132,839.11 inclusive of GST, plus interest and costs. For the reasons that follow, JSB's claim in conversion cannot succeed. There will be judgment for the defendants.

Factual Background

[4] During 2006, JSB supplied wool to Feltex from time to time. In late June 2006, JSB's insurer withdrew its credit insurance cover. This resulted in JSB and Feltex entering into a new written supply contract described as a "Feltex Mill Wool Supply Contract" which took effect from 1 August 2006 (the supply contract). In the lead up to the signing of the supply contract, Feltex's financial controller Ms Ursula South wrote to the JSB's chief financial officer on 2 August 2006, outlining key terms upon which Feltex would purchase certain of its wool requirements from JSB. These terms related to payment and were described in the letter as requirements placed on Feltex by JSB. As a result of the nature of the proposed terms, Feltex considered it could not commit to a supply arrangement beyond 31 October 2006.

The supply contract

[5] The supply contract was duly signed by the parties on 22 August 2006. It was intended that JSB supply wool to Feltex on a monthly basis, with the price to be established and advised each month according to a formula. Clause 4.0 dealt with terms of supply, relevantly stating that:

The contract shall be based on:

...

Payment will be made on a cash on delivery basis following presentation of documents.

1. JS Brooksbank & Co (“JSB”) are to supply a Certificate to confirm the following:

Upon the receipt of notification of cleared funds, unconditional ownership of the wool passes to the purchaser, Feltex Carpets Ltd (“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 are to be advised prior to the despatch of the wool.

[6] Points 1 and 2 were taken word for word from the letter of 2 August outlining the proposed terms of payment. Clause 7.0 contained some general provisions. Among these was subclause 6, which relevantly provided:

Price Basis

All wools will be purchased on the following basis:

...

- Payment: ~~Cash on delivery and presentation of documents~~ (delivery made on receipt [sic] of cleared bank funds).

[7] The amendment made by striking out the original text was in the handwriting of Mr Andrew Campbell, chief executive officer of JSB. Both copies of the supply contract contained the same amendment. The handwritten amendment was not initialled by the parties, but its inclusion as part of the supply contract has not been disputed.

[8] These terms of supply and delivery had been applied on behalf of Feltex since early August 2006 by its financial controller at the Foxton office, Ms South. For JSB it was contended, relying on the evidence of Ms South, that Feltex knew and understood that there was no possessory right to the wool until the cleared funds were received by JSB. Counsel for the receivers properly accepted at the hearing that officers of Feltex had such knowledge and understanding. The terms of supply and delivery outlined above were part of a commercial arrangement for which there were sound commercial reasons in the light of Feltex’s difficult financial circumstances.

[9] In any event, the supply contract required JSB to notify Feltex that it had received cleared funds. This is implicit from the requirements in point 1 in cl 4 (see [5] above). The next step was for JSB to send a Buyer Delivery Order (BDO) to the woolstores holding the wool on behalf of different wool brokerage houses. The BDO was the authorisation for the woolstores to release the wool to Feltex or Feltex's carriers. Mr Richard Carroll of JSB and various other deponents confirmed that it was only on confirmation that cleared funds had been received from Feltex that a BDO would be sent to the woolstores.

The ANZ debenture

[10] As a major lender to Feltex, ANZ entered into a composite debenture with Feltex in May 2000. The composite debenture was registered on the PPSR between 4 October 2002 and 23 June 2006 by filing several financing statements covering all present and after acquired property.

The transactions in dispute

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

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

[12] These invoices related to several different lots of wool held at different wool brokerages around the country. The Feltex accounts department submitted a bill funding note to ANZ in respect of the wool ordered for September delivery. A request was made to ANZ that payment be made on 4 September 2006.

[13] In early September 2006, Ms Angela Gust returned to work at the Kakariki scour having been on maternity leave since February 2006. She was the employee whose responsibilities included ordering and arranging transport for the wool. Ms Dawn Parkinson had been carrying out Ms Gust's role during her absence.

[14] Ms Gust deposed that on her return, she was generally informed of the new supply contract with JSB in what she described as a “quick catch up” conversation. She was informed that JSB required confirmation of payment before it would release the wool to the freight companies used by Feltex. She was not, however, told that payment for the month’s supplies had not yet been made. Ms Parkinson had left a set of orders for JSB on the desk marked “pick up for Tuesday”. The invoices had previously been brought to the attention of Feltex’s wool procurement manager Mr Berry. He did not authorise the wool pick up from the brokers. No instruction should have been given without his authorisation. However, Ms Gust deposed that she assumed payment had been made. She sent out faxed requests to each of the wool brokerages holding the relevant lots seeking release of the wool to the carriers. It is clear that Ms Gust was unaware that payment had not been made to JSB.

[15] On about 4 September, JSB personnel contacted Ms South from the Feltex office in Foxton to check whether payment for the wool had been made. Ms South confirmed that on 31 August 2006 she had requested that the ANZ do so, but she was unaware whether the funds had cleared. A day later, confirmation came through from ANZ to Ms South at Feltex in Foxton that the funds had not been cleared through to JSB. This was not, however, communicated within Feltex to the operators at the Kakariki scour.

[16] Not long after the facsimiles were sent requesting the release of the wool, some of the wool brokers contacted Ms Gust of Feltex to let her know that, as they had not received a BDO from JSB, they would not be releasing the wool. Similarly, some of the brokers made calls to the assistant accountant at JSB, Mr Drabble, to ask whether the wool should be released without a BDO. Mr Lawrence, JSB’s shipping manager, also received calls from some brokers advising that Feltex had requested the release of the wool. Both Mr Drabble and Mr Lawrence confirmed to those brokers who contacted them that cleared funds had not been received and the wool should not be released. Neither made contact with those brokers from whom they had not heard. Nor was any communication sent by JSB personnel to all brokers who were to supply wool product to Feltex reminding them of the requirement to have a BDO prior to the release of the wool.

[17] A number of brokers did release the wool on Feltex's request to Feltex's carriers, comprising a total of 24 lots, or some 246 bales, valued at \$132,839.11 including GST. This is the amount claimed by JSB. It is accepted that such wool was released by the brokers without a BDO having been received. The carriers delivered it to the Kakariki scour.

[18] Around 12 September 2006, Mr Berry of Feltex learned that the wool had been received by Feltex without having been paid for. He arranged for the wool to be put to one side and not be scoured. But he took no steps to ensure that JSB was paid, because he believed Feltex was about to be sold as a going concern to a third party.

[19] On 22 September 2006, receivers were appointed. That same day a representative of the receivers visited the Kakariki scour and discussed the plan to process all wool held there to facilitate trading Feltex as a going concern in order to on-sell the business. On September 25, the receivers' representative conducted a stock take at the scour, at which point it was realised that some of the wool acquired from JSB's brokers had not yet been paid for. The next day, the situation was discussed with JSB. JSB realised the precariousness of its position and lodged an *ex parte* application for an interim injunction, which was later withdrawn on the basis of an undertaking from the receivers in respect of damages.

[20] The above factual background was largely agreed between the parties. However, the order of events during the period prior to the delivery of the wool to the carriers was disputed. For example, there is some confusion over whether the wool brokers were in contact with JSB regarding the requests before they contacted Ms Gust. Feltex however accepted that JSB did not know that some of the wool had been released until contacted by the receivers on 26 September 2006.

[21] The exact sequence of events is not determinative of the case. Overall, the factual picture is one whereby Feltex personnel requested the release of the wool from the brokers without realising that it had not paid for that wool. Some wool was released by the brokers to the Feltex carriers, albeit without the requisite authority from JSB. I shall discuss these factual aspects further later in the judgment.

The claim

[22] This claim is to be determined on the evidence contained in the affidavits filed. JSB has applied for judgment against Feltex for conversion of its property. Feltex has submitted that the application for judgment should be declined because it has a good defence to the claim *inter alia* on the basis that the supply contract was a conditional sale agreement within the meaning of the term “security interest” under the PPSA. It was therefore subject to the priority of ANZ’s registered interest arising from the debenture.

[23] Rule 500 of the High Court Rules (the Rules) permits a proceeding to be determined on the basis of evidence contained in affidavits, provided that the parties file an agreement to follow that course. As is required by r 500(1), the parties have signed a formal agreement that evidence will be given by affidavit.

Submissions for JSB

[24] Mr Brant for JSB submitted that Feltex converted the wool by denying its possessory interest in, or title to, the goods. Feltex’s agents took the wool without any legal entitlement to do so as the wool had not been paid for. Mr Brant submitted that all the elements for the imposition of liability for conversion could be established. For liability for conversion to be established, the plaintiff must prove, as noted by Lord Nicholls of Birkenhead in *Kuwait Airways Corporation v Iraqi Airways Company (Nos 4 & 5)* [2002] 2 AC 883 at 1084 (HL), that the defendant’s conduct is inconsistent with the rights of the owner or other person entitled to possession. The conduct must also be deliberate. Further, the conduct must be so extensive an encroachment on the rights of the owner or other person as to exclude him or her from use and possession of the goods.

[25] Mr Brant submitted that there is no doubt that Feltex took the wool in denial of JSB’s possessory right and did so intentionally. Feltex’s continued retention of the wool despite requests for release also amounted to conversion.

[26] In response to the affirmative defence raised by Feltex under the PPSA, Mr Brant submitted that the PPSA does not apply in this case because JSB had no security interest in the goods as defined in the PPSA. Because Feltex had no right to an interest in the wool until payment was received, it could not at that stage be a debtor within the meaning of the PPSA. Hence, the wool could not be the subject of a security interest, meaning that the PPSA could not have been used to register the security. As a result, there is no defence to the claim of conversion.

[27] In any case, ANZ's interest could not attach to the wool pursuant to the composite debenture (as after acquired property), until Feltex had rights in the collateral. Because Feltex converted the wool, it had no rights in the collateral and thus the wool was not part of the personal property secured by the composite debenture.

[28] Finally, Mr Brant tentatively advanced the submission that the wool in the possession of Feltex, for which JSB had not been paid, might be subject to a constructive trust.

Submissions for Feltex

[29] Feltex opposed the application for judgment on the basis that JSB had an unperfected security interest in the wool. Ms O'Gorman submitted that JSB was purely another unsecured creditor in respect of the purchase price of the wool, an asset which was subject to the perfected security interest of ANZ in all Feltex's present and after acquired property. At the hearing, Ms O'Gorman responsibly abandoned an argument that JSB did not have title to the wool after possession passed to Feltex. That title remained with JSB in the present circumstances is clear from the terms of the supply contract.

[30] Ms O'Gorman submitted that while JSB retained title to the wool until payment under the supply contract, the crucial question is whether or not that agreement amounts to an arrangement securing payment, a security interest within the terms of the PPSA regime. She submitted that the ability to create security interests in assets that are not owned in the traditional sense by a debtor is

fundamental to the PPSA regime. Thus the regime covers conditional sale agreements on the basis that title is irrelevant: what matters is possession or control. Once a security interest covered by the PPSA is created by the parties, the registration and perfection of such security interest will result in the debtor obtaining priority.

[31] The fact that Feltex obtained possession of the wool without payment (albeit contrary to the agreed arrangement), amounts in Feltex's submission to either a waiver of the condition in the contract or to a mistake on JSB's part. Either way, debt is created and therefore a security interest exists in the goods. As this security interest is unperfected, it is subject to the priority of the perfected security interest of the ANZ in Feltex's present and after acquired property.

[32] Ms O'Gorman also made submissions supporting the proposition that liability had not been made out in conversion. Moreover, there was no legal or factual basis to support the existence of a constructive trust.

Issues

[33] For determination in the present case is whether there is a security interest in the wool within the terms of the PPSA. If there is, it becomes necessary to determine which party, having a security interest in the wool, possesses priority. If there is no security interest, then the essential question is whether Feltex converted the wool, making it necessary to look at whether JSB retained title to the wool and whether Feltex deliberately dealt with the wool in a manner inconsistent with JSB's rights. A further issue is whether there was a constructive trust over the wool.

Existence of a security interest

The PPSA regime

[34] The PPSA establishes a comprehensive personal property regime. Specifically, s 4 outlines that the PPSA mainly relates to:

- The enforceability of an interest in personal property created or provided for by a transaction that secures payment of money or performance of an obligation; the interest is called a security interest:
- How to determine the priority between security interests in the same personal property:
- How to determine the priority between a security interest and another type of interest (for example, the interest of a buyer of goods) in the same personal property.

[35] The PPSA was enacted in order to provide both a conceptually consistent regime for all personal property securities and to create a reliable, unified registry to give notice of, and to determine priority of, competing securities: see Widdup and Mayne in *Personal Property Securities Act - A Conceptual Approach* (revised ed 2002) at 1.2 to 2.6. To this end, a broad conceptualisation of the different types of personal property securities was developed. Hence, as identified by the Court of Appeal in *Waller v New Zealand Bloodstock Ltd* [2006] 3 NZLR 629 at [13] (CA), the key features of the PPSA involve:

...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.

[36] The central concept in the PPSA regime is therefore the security interest. It is defined in s 17:

17 Meaning of “security interest”

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

- (2) A person who is obligated under an account receivable may take a security interest in the account receivable under which that person is obligated.
- (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.

[37] The definition in s 17(3) specifically includes conditional sale agreements, including an agreement to sell subject to retention of title. In *Simpson v New Zealand Associated Refrigerated Food Distributors Ltd* [2007] 2 NZLR 130, the Court of Appeal approved of the decision of Goddard J at first instance in *Service Foods Manawatu Limited (in rec & liq) & Ors v NZ Associated Refrigerated Food Distributors Limited* (2006) 9 NZCLC 263,979. At [21], the Judge stated:

...it is the substance of an arrangement securing payment or performance of an obligation that is contemplated by s 17 rather than the form of the arrangement...

[38] It is clear from the terms of s 17(1)(a) that the issue of title is non-determinative. As Widdup and Mayne put it at 2.11:

...the PPSA resolutely disregards title, with the effect that merely holding title to a collateral in an effort to secure payment or the performance of an obligation is no longer effective. While this feature of the PPSA will present a conceptual hurdle to many, it clearly identifies that title retention arrangements are security interests.

[39] Section 24 is specific on this point: the application of the PPSA is not affected by the secured party having title to collateral. The section provides:

The fact that title to collateral may be in the secured party rather than the debtor does not affect the application of any provision of this Act relating to rights, obligations, and remedies.

[40] Therefore, once a security interest has arisen (thereby making the vendor a secured party), the fact that the secured party holds title to the goods means little. This legislation, while not a complete code, is intended to govern the great majority of dealings with personal property. Section 23, for example, identifies a number of specific situations (such as a seller's interest in goods shipped under a negotiable bill of lading) in which the PPSA *does not* apply.

[41] One requirement of granting a security interest in the collateral (in this case the wool which comprises goods as defined in s 16), is the need for a debtor to have rights in the collateral. This is outlined by s 40:

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.
- (2) Subsection (1) does not apply if the parties to a security agreement have agreed that a security interest attaches at a later time, in which case the security interest attaches at the time specified in the agreement.
- (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.
- (4) To avoid doubt, a reference in a security agreement to a floating charge is not an agreement that the security interest created by the floating charge attaches at a later time than the time specified in subsection (1).

[42] The application of the provisions of s 40 in the context of this case will be discussed later. A security interest may be perfected or unperfected. Both of these are defined terms in s 16:

perfected security interest, in relation to a security interest, means the security interest is perfected by possession or by registration or is temporarily perfected, as the case may be:

unperfected security interest means a security interest that is not a perfected security interest:

[43] To complete the definition of perfected security interest, under s 16 “perfected by possession” is also defined:

perfected by possession, in relation to a security interest, means the security interest has attached and the secured party has taken possession of the collateral (except where possession is a result of seizure or repossession)

[44] Section 16 also defines “debtor” and “secured party”:

Debtor –

(a) Means –

- (i) A person who owes payment or performance of an obligation secured, whether or not that person owns or has other rights in the collateral; or
 - (ii) A person who receives goods from another person under a commercial consignment; or
 - (iii) A lessee under a lease for a term of more than one year; or
 - (iv) A transferor of an account receivable or chattel paper; or
 - (v) A transferee of or successor to the interest of a person referred to in subparagraphs (i) to (iv); or
 - (vi) If the person referred to in subparagraph (v) and the person who owns or has other rights in the collateral are not the same person, includes –
 - (A) The person who owns or has other rights in the collateral, where the term “debtor” is used in a provision of this Act dealing with the collateral; or
 - (B) The obligor, where the term “debtor” is used in a provision of this Act dealing with the obligation; or
 - (C) Both the person who owns or has other rights in the collateral and the obligor (if the context so requires); and
- (b) Includes a trustee for any of the persons referred to in paragraph (a):

Secured party –

- (a) Means a person who holds a security interest for the person's own benefit or for the benefit of another person; and
- (b) Includes a trustee where the holders of the obligations issued, guaranteed, or provided for under a security agreement are represented by a trustee as the holder of the security interest:

[45] “Collateral” is also a defined term in s 16:

collateral means personal property that is subject to a security interest:

[46] Personal property has a further definition in that section:

personal property includes chattel paper, documents of title, goods, intangibles, investment securities, money, and negotiable instruments

[47] Possession is also a crucial concept in the present case. Section 18 defines possession in certain cases, including that outlined in subsection (3):

- (3) For the purposes of this Act, a secured party is not in possession of collateral that is in the actual or apparent possession or control of the debtor or the debtor’s agent.

Discussion

[48] The starting point for the analysis is to consider the definition of security interest in s 17 as applied to the facts of the case. JSB disputes that this is a transaction securing payment or performance of an obligation. Further, it is said there was no agreement by JSB that possession should be obtained by Feltex. It was submitted this is required by the need for consensus outlined in *Re King Robb Ltd (in liq); Sleepyhead Manufacturing Co Ltd v Dunphy & Anor* (2006) 9 NZCLC 264,000 (HC) (upheld on appeal in *Dunphy & Anor v Sleepyhead Manufacturing Co Ltd* [2007] 3 NZLR 602 (CA)). JSB relies on the observation of Harrison J in at [38] to the effect that the purpose of the PPSA:

...is to provide a uniformity of treatment of all consensual security interests in personal property which is not dependent upon the form of the transaction.

[49] I consider that the use of the word “consensual” in that case does not have the meaning for which JSB contends. There is no suggestion in the judgment of Harrison J that the possession of the collateral must be consensual; the focus was on the transaction in question. In *Widdup and Mayne*, the need for security interests to be consensual is discussed at 2.15 where it is stated that:

The interest in the personal property must be created by a consensual transaction. In other words, the debtor must agree to provide the interest in the personal property to the secured party.

[50] Gedye, Cuming and Wood in *Personal Property Securities in New Zealand* (2002) at 17.4 also acknowledge the need for the interest to arise consensually as one of three prerequisites to the PPSA’s operation. But there is no suggestion that possession of the collateral is an integral part of the analysis. Indeed, that would be surprising given that the PPSA itself contains provisions relating to possession, such as s 18.

[51] Consensus (in relation to whether a security interest is created) arises in a different context to that which applies in the current case. The requirement for consensus is to prevent registration of interests arising by the operation of law or being imposed unilaterally on the debtor by the creditor. There is no specific requirement in the commentaries or the law that mandates that the creditor

additionally agree to the possession of the goods by the debtor. In this case, there was an agreement to buy and sell certain goods. Although the supply was not carried out in the manner anticipated in the supply contract, once wool was supplied by JSB to Feltex there was a debt, an obligation to pay, that the debtor Feltex agreed to meet.

[52] The application of the principles in s 17 suggests that the arrangement embodied in clause 4 of the supply contracts falls squarely within the definition of conditional sale agreement. As a matter of fact, I find that the commercial arrangement here, as set out in the supply contract, involved an agreement to sell wool subject to the retention of title. The consequence is that a security interest as defined by s 17 of the PPSA has been created: see s 17(1)(a).

[53] This approach is consistent with decision of Judge Mathers in *Segard Masurel (NZ) Ltd v Nicol & Ors* DC AK CRI 2006-004-3020 23 May 2007. That case involved another of Feltex's wool suppliers. The usual terms of that supply were cash on delivery. In September 2006, the plaintiff supplied over \$350,000 worth of wool to Feltex. Some of this debt was eventually paid before Feltex went into receivership, but a significant portion was left outstanding.

[54] The Judge acknowledged that (unlike the present case) the contract was silent on the issue of whether title was retained. She found that, although the arrangement began as 'cash on delivery', on this particular occasion by tacit or actual agreement credit was given to Feltex. Judge Mathers concluded that title passed at the time of delivery. She added at [30] that, even if that were wrong, retention of title would constitute a security interest. The agreement was in the nature of a conditional sale agreement and therefore covered by the PPSA. At [26] she stated:

In my view by deeming a retention of title clause to be a security interest, the asset in question is effectively vested in the debtor. Once this occurs the Act provides for the determination of the priorities.

Therefore the debenture held by ANZ had priority, catching the collateral, being all present and after acquired property.

[55] Plainly there are factual differences between that case and the present. There, the supply of the wool occurred consensually even though the cash on delivery

clause was not met. But I consider that the outcome will be the same. If, by some mistake or agreement, possession of the wool is passed, a debt will have been created and credit given: there would exist a security interest that falls within the terms of s 17. The fact that title has been retained under the supply agreement merely underscores such characterisation.

[56] In the present case, it is clear that Feltex obtained possession of the wool when JSB's brokers released the wool to Feltex's carriers: see s 18(3). Further, so far as JSB is concerned, attachment of the security interest would have arisen when the debtor (Feltex) had rights in the collateral: see s 40(1)(b).

[57] The means of determining when this occurred is provided by s 40(3). Here, it may be said that the wool was either consigned to Feltex as the debtor or sold to Feltex under an agreement to sell subject to retention of title. In each case, attachment of a security interest to the collateral would occur "no later than when the debtor obtains possession of the goods".

[58] JSB submitted that Feltex could not be a debtor for the purposes of s 40 because Feltex did not meet the criteria of debtor: the supply contract did not secure an obligation. However, I consider that this argument is unpersuasive. Inevitably, if a security interest exists (as I have found), there will be a debtor within the meaning of that term in s 16, if and when goods are supplied. This view derives support from Widdup and Mayne at 12.2. It is there noted that:

A "debtor" will always be one of the parties to any transaction that falls within the definition of "security interest". In addition to persons who grant a security interest in personal property and who owe payment or performance of an obligation, a debtor is a person who receives goods from another person under a commercial consignment... These persons are specifically identified and included within the definition because these transactions are not in substance security interests. As deemed security interests subject to the PPSA, these consignees, lessees, and transferors do not owe payment or performance of an obligation that is secured by collateral, but are nevertheless debtors under the PPSA and provisions that apply to debtors will apply equally to these persons because they are included within the definition.

[59] Mr Brant also sought to argue that the transaction did not involve a security interest because of the introductory words to s 17. He relied on the phrase "unless

the context otherwise requires” to suggest that the Court could analyse a factual situation and then determine whether the context otherwise required that no security interest be found to exist. He submitted that, as it was never envisaged by the parties that possession of any wool would be released without payment being made, the provisions of the supply contract did not give rise to a security interest.

[60] I disagree. It is important to appreciate that an “in substance” approach is called for by s 17(1). Plainly, cl 4 and the other provisions of the supply contract embodied a transaction that in substance secured payment or performance of an obligation in respect of future sales of wool. More particularly, such a transaction involved a conditional sale where there was an agreement to sell wool subject to retention of title until certain events occurred. In those circumstances, I can find no contextual factors (including other relevant provisions of the PPSA) which would warrant a requirement that the provisions of s 17 not apply.

JSB’s options

[61] When the parties entered into the supply contract, JSB tried to protect its interest by requiring payment before delivery. However, it was unsuccessful in doing so in the circumstances which eventuated. However, retention of title no longer has the same significance it once did prior to the PPSA. JSB had the option of perfecting its security interest by registration. Once perfected, it would have amounted to a purchase money security interest (PMSI), as defined in s 16:

purchase money security interest—

(a) Means—

- (i) A security interest taken in collateral by a seller to the extent that it secures the obligation to pay all or part of the collateral's purchase price; or
- (ii) A security interest taken in collateral by a person who gives value for the purpose of enabling the debtor to acquire rights in the collateral, to the extent that the value is applied to acquire those rights; or
- (iii) The interest of a lessor of goods under a lease for a term of more than 1 year; or
- (iv) The interest of a consignor who delivers goods to a consignee under a commercial consignment; but

(b) Does not include a transaction of sale and lease back to the seller:

[62] A PMSI takes priority over a perfected security interest in all present and after acquired property, if it is registered within 10 days of the debtor obtaining the collateral, as set out in s 73 of the PPSA. Therefore, had the security interest been promptly registered on the PPSR, JSB would have retained priority over the composite debenture. That is because PMSI creates what is known as a form of “super-priority”.

Conversion

[63] As outlined by counsel for JSB, the *Kuwait Asia Bank* case defines the essential elements of the tort of conversion at 1084. Proof of the following elements is required:

- i) The defendant’s conduct must be inconsistent with the rights of the owner or other person entitled to possession;
- ii) The conduct must be deliberate; and
- iii) The conduct must be so extensive an encroachment on the rights of the owner or other person as to exclude him or her from use and possession of the goods.

[64] It is clear that Feltex’s carriers action in obtaining the wool from JSB’s brokers was conduct inconsistent with JSB’s rights as the owner and party entitled to possession of, and title to, the wool. That action also excluded JSB from use and possession of the wool. As a result, the argument regarding conversion centred around whether the conduct of Feltex was deliberate.

[65] Whether conduct is deliberate was discussed in Todd *The Law of Torts in New Zealand* (4 ed 2005) at 12.3 (omitting footnotes):

Conversion is an intentional wrong. This means that the defendant must intend to do the act which constitutes the denial of the plaintiff’s rights. The conduct must therefore be deliberate and not accidental. The defendant’s intention is taken to include also the natural and probable consequences of

those actions which are intended in fact. This is so even if such consequences may have been unintended and even undesired.

[66] However, there is clear authority that a voluntary delivery of goods does not constitute conversion. In *PGG Wrightson Ltd v Wai Shing Ltd & Anor* HC AK CIV 2003-404-006579 23 February 2006, Keane J dealt with a claim in conversion where the defendants were said to have converted goods delivered to them by an allegedly fraudulent employee of the plaintiff. Keane J held at [55]-[56]:

The essence of conversion may lie in WSL and HBC having come into possession of product inconsistently with Fruitfed's rights, whether or not they were alive to that: *Wilson v New Brighton Panelbeaters* [1989] 1 NZLR 74, at 80, *Central Acceptance Ltd v Smith Hughes & Robertson* [1992] 3 NZLR 413, CA, at 415. But Fruitfed delivered to WSL or HBC the product on which its claim depends under contracts it has never repudiated, and seeks rather an increased price.

That is fatal. Voluntary delivery displaces conversion, even when induced by fraud: Todd *'The Law of Torts'*, 4th edition, para 12.3.01, page 469. And Fruitfed stops short of attributing fraud to WSL or HBC. It attributes fraud to Mr Dark.

[67] A voluntary transfer of possession from the agent of the vendor to the buyer cannot amount to conversion because it is a lawful transfer. In *Jeffcott & Anor v Andrew Motors Ltd* [1960] NZLR 721 (CA), Mr and Mrs Jeffcott negotiated the sale of a car to a Mr Steven. He returned to the Jeffcotts' house and gave Mrs Jeffcott a fake cheque for the sale price. In return, Mrs Jeffcott gave him the car. The Court considered this to be a voluntary transfer of possession. Mr Steven sold the car to a third party, Andrew Motors Ltd. While the contract with Mr Steven may have been voidable because of fraud, Mrs Jeffcott's delivery of the car was still by consent. The present is an even stronger case for a voluntary transfer of possession as there was no fraud or other deliberate deception involved.

[68] In *Dennant v Skinner & Collom* [1948] 2 KB 164 property in a vehicle sold at auction passed when the auctioneer brought down the hammer, but with the auctioneer retaining a right to possession until payment was made. The buyer, who the auctioneer mistakenly thought was a reputable dealer, convinced him to allow payment by cheque. At this point, the buyer was given possession of the vehicle. Hallett J found at 172:

...once [the auctioneer] chose, for reasons good, bad, or indifferent as a result of statements fraudulent or honest, to part with the possession of the vehicle by giving delivery of it, he then lost his seller's lien and no longer had a right to possession of the vehicle.

[69] Here, JSB's agents voluntarily delivered the wool to Feltex's carriers. While JSB itself did not intend to deliver the wool, the actions of the agent are attributable to the principal. Therefore, it is quite clear that in the present case possession was voluntarily transferred, defeating a claim of conversion. The claim in conversion must fail.

Constructive trust

[70] Although it was not pleaded, counsel for JSB suggested during argument that the wool may have been held on a constructive trust by Feltex. A constructive trust may be imposed over property which is held by a person in circumstances where it would be inequitable to allow him or her to assert full beneficial ownership of the property (see *Laws NZ "Trusts"* at paragraph 484). Constructive trusts are remedial in nature, equitable instruments that force the disgorging of property in circumstances where it is unconscionable or contrary to fundamental equitable principles for the owner of particular property to hold it purely for his or her own benefit.

[71] In *Fortex Group Ltd (In Receivership and Liquidation) v MacIntosh* [1998] 3 NZLR 171 (CA), Tipping J stated at 175 (for the majority) that unconscionability is a requirement of a remedial constructive trust:

Equity intervenes to prevent those with rights at law from enforcing those rights when in the eyes of equity it would be unconscionable for them to do so. Equity acts in this respect as a Court of conscience. In order to defeat, pro tanto, the secured creditors' rights at law under their security by the imposition of a remedial constructive trust, the plaintiffs must be able to point to something which can be said to make it unconscionable – contrary to good conscience – for the secured creditors to rely on their rights at law. If such can be shown, equity may restrain the exercise of those rights to the extent necessary to afford the plaintiffs appropriate relief.

[72] The basic conceptual problem faced by JSB in attempting to assert that a constructive trust arose over the wool in Feltex's possession is that there is no

evidence of unconscionability in the present case. As is demonstrated by the circumstances described at [11] to [20] above, this was a case which involved a succession of genuine mistakes by personnel within Feltex, by the brokers as agents of JSB, and possibly even by employees within JSB itself. JSB was on notice that Feltex was seeking to obtain delivery of the September wool requirements from brokers, even though the brokers had not received a BDO from JSB. But there was no deliberate attempt by Feltex to obtain the wool by unconscionable means. As earlier described, JSB through its agents gave delivery of the wool voluntarily to Feltex. JSB faces an insurmountable problem in the face of the maxim that equity will not assist a volunteer.

[73] In *Powell v Thompson* [1991] 1 NZLR 597 (HC) Thomas J, in dealing with an alleged constructive trust, noted that the definition of a constructive trust is not a settled concept. He continued at 606:

Suffice to say that various criteria have been recognised in different decisions and in different jurisdictions. However, whether the juristic basis has been expressed in terms of unconscionability, constructive or equitable fraud, unjust enrichment, imputed intention, denial of reasonable expectations, or proprietary or promissory estoppel, the outcome is the same; the Courts will declare the defendant to be a constructive trustee of the property in question whenever, in all the circumstances of the particular case, it is perceived that it would be unjust or unfair not to do so. Almost invariably the element which underlies the finding is the unmerited enrichment of the defendant at the expense of the plaintiff.

[74] At 607, Thomas J discussed the requirement of knowing receipt as an element of a constructive trust. Hence, JSB would need to establish that Feltex must have known that it was obtaining an advantage at JSB's expense. Again, my finding that there was no unconscionability or deliberate conduct on Feltex's part is fatal to the claim of unjust enrichment. The contention that Feltex held the wool under a constructive trust cannot succeed.

Result

[75] For the reasons outlined above, the claim by JSB under the tort of conversion fails. I have also found that there is no basis in the circumstances of this case giving rise to a constructive trust.

[76] The provisions of the supply contract created a security interest within the meaning of s 17 of the PPSA. If JSB had wished to achieve super priority in respect of any wool to be supplied pursuant to the supply contract, it should have registered the security interest as a purchase money security interest under s 73 of the PPSA. It did not do so. Contrary to the arrangements in the supply agreement, wool was released into the possession of Feltex. Such wool was thereafter to be treated as after acquired property and covered by the ANZ composite debenture which had been registered under the PPSA. Therefore, it had priority over the unperfected security interest of JSB. On that basis, the affirmative defence raised by the defendants must succeed.

[77] Accordingly, the plaintiff's claim fails. There will be judgment in favour of the first and second defendants. The defendants are entitled to costs which should, unless the parties wish to argue otherwise, be calculated on a 2B basis.

Stevens J