IN THE HIGH COURT OF NEW ZEALAND
PALMERSTON NORTH REGISTRY

708

A.101/77

BETWEEN SOUTH PACIFIC CONSTRUCTION LIMITED a duly incorporated company having its registered office at 105 Princess Street, Palmerston North and carrying on business at Palmerston North and elsewhere as contractors

Plaintiff

A N D NEWBURY CONSTRUCTION COMPANY LIMITED (In Liquidation) a duly incorporated company having its registered office at the offices of Messrs Barr Burgess & Stewart, Chartered Accountants, Fourth Floor, Library Building, The Square, Palmerston North

First Defendant

A N D THE MAYOR COUNCILLORS AND CITIZENS OF THE CITY OF PALMERSTON NORTH a body corporate under and by virtue of the Municipal Corporations Act 1954

Second Defendant

Hearing: 29 April 1981

Counsel: C.J. Walshaw for Plaintiff
J.C.A. Thomson for Defendants

Judgment: - 7 OCT 1981

JUDGMENT OF HARDIE BOYS J.

By written contract dated 22 December 1976, the first defendant ("Newbury") agreed to build a block of pensioner flats for the second defendant ("the Council"). Before the work was complete, Newbury was put into liquidation by order of this Court made on 7 September 1977. The Official Assignee was appointed provisional liquidator and was subsequently replaced by two chartered accountants in public practice in Palmerston North who in contrast with the Official Assignee I shall call "the liquidators".

Between the date of the winding-up order and the appointment of the liquidators the work was carried on by the plaintiff ("South Pacific"). South Pacific claims $19,973 for the work it did. It has not been paid. Neither defendant has yet admitted that the amount of the claim is a proper one, but that matter has been left over pending the decision I have been asked to make, which is essentially whether either of the defendants is liable at all.

The plaintiff brings its claim on alternative grounds. First, it says that the arrangements that were entered into constituted either a new contract between it and the Council, or an assignment to it of Newbury's contract with the Council, so that the Council is directly liable for the work that was done. Alternatively, it says that it became a subcontractor of Newbury, and consequently is entitled to a charge under the Wages Protection & Contractors Liens Act 1939 (but not a lien - s 50) on moneys payable by the Council to Newbury. The Council's response to the claim is that South Pacific's contractual arrangements were made between it and Newbury, and did not involve an assignment. If those arrangements were such as to entitle South Pacific to a charge under the Act, there is no fund to charge, for no further moneys are payable to Newbury. The attitude of Newbury's liquidators as I understand it is that the arrangements that South Pacific entered into were made with the Official Assignee and are not binding on them.

Newbury's contract with the Council incorporated the General Conditions of Contract published as NZSS 623:1964, clause 19.1 of which entitles the principal, in the event inter alia that a winding-up order is made, either to take possession of the works and complete them itself, or to determine the contract. However, it appeared to the major creditors that the contract was capable of profitable completion, and accordingly it was agreed at a meeting of creditors held immediately after the winding-up order was made, at which the Official Assignee was present as provisional liquidator, that an approach should be made to the Council to obtain its approval to the contract being continued through to completion. The Official Assignee obtained

an indemnity from the major creditors in these terms:

> " 7 September 1977
>
> The Official Assignee,
> Commercial Affairs Division,
> Private Bag,
> NAPIER.
>
> Dear Sir,
>
> NEWBURY CONSTRUCTION LIMITED (IN LIQUIDATION)
>
> In forebearance of my request that you continue to operate the business of the company pending the appointment of a Liquidator, I hereby indemnify you against all costs, charges, expenses and any possible claims for damages which might arise out of your continuing to operate the business.
>
> Yours faithfully, "

The Official Assignee then appointed Mr Jobberns, local manager of one of the major creditors, who had carried out the assessment on which the creditors' decision was based, to act as his agent as he was himself based in Napier. Mr Jobberns' appointment was confirmed in a letter from the Official Assignee in which it was stated that the purpose of the appointment was "protecting assets and any other property of the company". Mr Jobberns immediately discussed the matter with one of the Council's engineers and then wrote to the Council to put the creditors' proposal formally before it. The letter said: (8 September 1977)

> "It is the opinion of the Official Assignee, that as his agent I should make arrangements to continue work on the contract now that liquidation has been served so that work may continue and all suppliers, of course, would be paid on a preferential basis from this point."

Then, after pointing out the advantage to the Council of not having to recall tenders, it went on:

> "As Agent to the Official Assignee I am empowered to continue the contract meantime and in confirmation of our discussion yesterday, have already made arrangements for work force to be employed and for the site to be secured meantime."

The Official Assignee followed up this letter the next day with one of his own, in which he stated to the Council:

> "...naturally the creditors of the company are desirous of completing the contract rather than substaining further losses.
>
> This letter is to reinforce the representations which have been made to you by Mr Jobberns and to seek your confirmation that favourable consideration can be granted as soon as possible to this request as Mr Jobberns is in a position to make immediate arrangements for the work to be resumed.
>
> Mr Jobberns has my full authority to act as my agent in Palmerston North on this matter ..."

These requests were considered by the Council at a meeting on 15 September and on that day its decision was conveyed to Mr Jobberns in a letter which contained these words:

> "...I am authorised to advise that approval is given for work on the Corporation's Senior Citizens Housing Contract No.1140 in Russell Street to resume forthwith under the direction of the Official Assignee and Provisional Liquidator delegated, as advised, to yourself.
>
> It is to be accepted and understood, of course, that all work included in the contract is to be carried out in strict compliance with the documents relative to the contract between the Corporation and Newbury Construction Ltd. now in liquidation.

> May I express the confident expectation that the contract will be carried to an early and satisfactory conclusion and that the outcome will be to the mutual satisfaction of the Corporation and the creditors concerned."

No mention of South Pacific was made in this correspondence. However, Mr Jobberns had ascertained that that company would be able to undertake the work without delay, and after the Council had approved its resumption, Mr Jobberns obtained authority for it to be undertaken by South Pacific. On 19 September, Mr Jobberns, signing as "agent for Official Asignee and Provisional Liquidator" wrote to South Pacific in these terms:

> "As the appointed agent of the Official Assignee to the above contract, I am authorised to confirm discussions held between us recently whereby your company has agreed to undertake completion of the works in accordance with issued plans and specification. You are authorised to enter upon the site and make necessary contractual arrangements to execute the prompt completion of the contract."

Mr Jobberns had not at this stage seen the documents which constituted the contract between the Council and Newbury, apart from the plans. He said he did not discuss with South Pacific the manner in which that company was to be paid for its work. In evidence, the reason he gave was "I could not instruct the City Council how they were to pay their contractors." He said that by the last sentence of his letter of 19 September, he meant that "I wasn't aware of the original contract arrangements between the Council and Newbury, any subsequent arrangements would have to be those made between incoming contractor and main party which is the Council - I was in fact placing the onus for that upon South Pacific."

Mr Jobberns' memory was at fault however, because the then manager of South Pacific said in evidence that he had discussed payment with Mr Jobberns who confirmed "costs to be recovered on a cost plus percentage basis (say 7½%) until directed otherwise by eventual official Liquidator, South Pacific, to submit progress claims direct to Quantity Surveyor and payment to be made via Liquidator." It is clear that South Pacific was satisfied that it would be paid, and that payment would come from the Council, either direct or through the Official Assignee. That was as far as South Pacific's concern went and there is no evidence to show that those of its officers who were involved applied their minds at all to the nature of the contractual arrangements that were being entered into. The belief that payment would come from the Council takes the matter no distance at all. The Council was indeed the ultimate payer, whatever the arrangements were for having the work completed.

The officers of the Council who were involved understood the position to be that the contract with Newbury was continuing notwithstanding the winding up, and that South Pacific was doing the work on behalf of the Official Assignee and the creditors. Their belief was exemplified by a written instruction to their Quantity Surveyors, dated 29 September 1979, which referred to South Pacific "who are working on this contract for the Official Assignee". Nonetheless, they dealt direct with South Pacific over such matters as work orders and contract variations. I do not regard that as significant. Mr Jobberns had dropped out of the picture once South Pacific were on the job and the Official Assignee was stationed in Napier. It was obviously simpler and quicker to deal direct with the builder on the job.

The Council's view was shared by at least one of those who attended the initial creditors' meeting on 7 September. His evidence was that the meeting asked the Official Assignee to negotiate continuation of the

contract because it was expected there would be a profit margin sufficient even to pay the creditors in full. He said "The provisional liquidator, he was authorised by creditors to complete the contract." It was for this reason that he signed the form of indemnity that I have referred to.

On 6 October 1977, South Pacific submitted a first progress payment claim. The accompanying letter stated:

> "We enclose herewith a progress claim for work completed to date on the above contract, on behalf of the Official Assignee for Newbury Construction Ltd (In Liquidation).
>
> Henceforth it is our intention to submit a claim at the end of each month direct to your Quantity Surveyors, Holmes Cook Hogg and Cardiff.
>
> We would appreciate early receipt direct to this office of your Certificate, followed by payment in due course by the method arranged."

As I understand it, the last sentence is not a reference to a method of payment which to the writer's knowledge has already been arranged. The point was that it was still to be decided whether payment was to be made direct or via the Official Assignee.

The progress claim was checked by the Council's Quantity Surveyors and approved. The Engineer then certified it for payment. The certificate showed the contractor as "Newbury Construction Ltd (In Liquidation) C/- Official Assignee, Department of Justice, P.B. Napier", and read "I certify that $7,276.21 is now due in accordance with the contract and is payable to Official Assignee, Napier."

In accordance with the contract, this payment was due by 27 October. However, on 12 October the Official Assignee had been replaced by the liquidators. They, with

receive would be the value of the work completed to date as certified by the Engineer under cl 19.2.2 of the General Conditions. No doubt a direct arrangement between South Pacific and the Council would have been beneficial to creditors had there been a risk that completion by some other contractor at a greater cost would have resulted in inroads on the value of work completed by Newbury. (cl 19.2.3). However, it is clear that the creditors were not acting to prevent a deficiency or even to preserve the value of work completed, but to secure additional funds by completing the work themselves. Such a result could be achieved only by Newbury remaining the contractor.

Nonetheless, Mr Walshaw argued that there had been a novation, whereby the contract between Newbury and the Council was extinguished and replaced with a new contract between South Pacific and the Council. Novation of course requires the consent of all the parties, although this consent may be inferred from acts and conduct (Chitty on Contracts General Principles, 24 Ed para 1193). However, care must be taken in the extent of resort to acts and conduct, and to words too, for the law is quite clear that "it is not legitimate to use as an aid in the construction of the contract anything which the parties said or did after it was made" (Miller v Whitworth Street Estates Ltd /1970/ AC 583, 603 per Lord Reid. See also L.Schuler A.G. v Wickman Machine Tool Sales Ltd /1973/ 2 All ER 39, where Lord Morris of Borth-y-Gest gave as reason for this rule that "if on the true construction of a contract a right is given to a party, that right is not diminished because during some period either the existence of the right or its full extent was not appreciated." (p 52)).

In order to ascertain whether there was indeed a novation, it is necessary to look at such contractual documents as there are, in order to ascertain the intention of the parties at the time the arrangements were entered into. It is not permissible to consider their subsequent actions, nor of course their statements in the course of negotiation.

Intention is to be derived, not from extrinsic evidence, but on legal principles of construction, from the words the parties have used. (Schuler's case per Lord Wilberforce p 53). However, as Lord Wilberforce observed in the earlier case of Prenn v Simmonds /1971/ 3 All ER 237, 240, 241, the words are not to be "isolated from the matrix of facts in which they were set and interpreted purely on internal linguistic considerations." The Court is entitled, indeed required, to "enquire beyond the language and see what the circumstances were with reference to which the words were used, and the object, appearing from those circumstances, which the person using them had in view." But evidence "should be restricted to evidence of the factual background known to the parties at or before the date of the contract, including evidence of the 'genesis' and objectively the 'aim' of the transaction". Neither of these were novation cases, each involving only the construction of a written agreement. The elements relevant to novation are slightly more extensive, for it is not a matter of ascertaining the intention of only two contracting parties, but of three. All three must assent to the "rescission of one contract and the substitution of another in which the same acts are to be performed by different parties" - that being of the essence of novation (Chitty para 1375). "The question in every case is one of fact, and in order to establish novation there must be the animus novandi, and the substitution of some other thing for the original obligation or debt" (Nelson Diocesan Trust Board v Hamilton /1926/ NZLR 342, 349 per Sim J (CA)).

I have already referred to the 'genesis' and 'aim' of the contract which South Pacific entered into. In my opinion, it is inconsistent with novation. Moreover, the correspondence between the Official Assignee and his agent Mr Jobberns on the one hand, and the Council on the other, clearly contemplated a continuing contractual relationship between Newbury and the Council, whilst the letter of 19 September from Mr Jobberns to South Pacific

is in terms of an agreement between Mr Jobberns as agent of the Official Assignee and South Pacific. The second sentence of that letter, quoted above, is doubtless equivocal but in the total context I do not regard it as an invitation to South Pacific to enter into a new contract for it is clearly the existing contract that is referred to in terms of prompt completion. I think the words "contractual arrangements" mean no more than "arrangements in accordance with the contract." Mr Walshaw also placed some reliance on the second of the paragraphs I have quoted from the Council's letter of 15 September. However I do not think the words used indicate that a new contract has been created. They confirm that South Pacific was to do what Newbury was to have done, but that is consistent with both possibilities. The general tenor of the correspondence is thus, in my opinion inconsistent with a novation.

Mr Walshaw submitted that this case was similar to Re Marton Club House Buildings Co Ltd (1908) 10 GLR 582 and Cooke Heating Ltd v The Auckland Grammar School Board an unreported decision of Chilwell J (Auckland A 510/73, 24 August 1978). These cases are helpful, particularly the latter for its very full exposition of novation, but they do not help the plaintiff in this case. Each case depends on its own facts and the facts in those cases are very different from those in this. The difference between this case and the Cooke Heating case is very instructive, for in that case there was clearly present the necessary intention on the part of the three parties concerned, in marked contrast with the present where that intention is manifestly absent.

The reason Mr Walshaw argued for novation was in part that his client did not wish to be bound by the contract price and schedule rates set out in the Newbury contract, but instead wished to recover on a cost-plus basis. There would have been difficulties about that too, for there was no evidence that any terms had been agreed other than those in the original contract documents, except in the minor respects in which variations to the

works had been expressly approved.

As an alternative to novation, Mr Walshaw argued that there had been an assignment of Newbury's contract to South Pacific. Assignment developed in equity as a means of avoiding the necessity for consent which applies to novation. However, the contract itself may stipulate for the consent of the other party to be obtained before a party can assign. In that event, a purported assignment, whatever its effect may be between assigner and assignee, is not effective vis-à-vis the other original contracting party. (Chitty para 1172). In the present case, clause 7.1 of the General Conditions states:

> "The contractor shall not assign the contract or any part thereof or any benefit or interest therein or thereunder without the written consent of the Principal."

The parties also executed a document headed "Agreement for Fulfilment of Contract" which provides that clauses 2 to 6 of the Fifth Schedule to the Municipal Corporations Act 1934 shall be deemed to form and be read and construed as part thereof. Clause 2 of this Schedule states:

> "The contractor shall not assign or make over his contract to any person without the previous consent in writing of the Council."

I understood Mr Walshaw to submit that the contract actually permitted assignment, but I cannot see how that can be so in view of the provisions I have quoted. If he was relying on the definition of "Contractor" in the General Conditions, which includes inter alia the assigns of the successful tenderer, then the answer is clearly that this definition is to be read subject to the express provisions mentioned, and is to be read restrictively so as to refer to "permitted assigns".

Mr Walshaw next argued that the Council's letter of 15 September 1977 amounted to a consent to assignment. I cannot agree. That letter must be read in the light of the letter to which it was a reply, namely Mr Jobberns' letter of 8 September and the Official Assignee's of 9 September. Neither of these makes any reference to an assignment. Mr Jobberns' letter said that he was continuing the contract as agent for the Official Assignee, whilst the latter's said that the creditors were desirous of completing the contract. There is no application in these letters for consent to an assignment, and the Council's reply cannot in my view be construed as consent.

That there was not an assignment is I think clearly established by the evidence of Mr Phillips of South Pacific who said that in his discussion with Mr Jobberns it was arranged that South Pacific was to be paid on a cost plus basis. That was a quite different basis from that provided by the contract.

The result of the conclusions to which I have come is that South Pacific had no contractual relationship with the Council. Its rights were with Newbury. There can be no doubt that the Official Assignee as provisional liquidator was exercising the power conferred on him by s 240(1)(b) of the Companies Act to "carry on the business of the company, so far as may be necessary for the beneficial winding up thereof." The Council had not exercised its powers under Clause 19.1 of the General Conditions, so the contractual relationship between it and Newbury continued unimpaired. South Pacific therefore became a subcontractor of Newbury, entitled to exercise the rights of a subcontractor conferred by law. These include the right to a charge under the Wages Protection and Contractors' Liens Act 1939. This much, I gather, is acknowledged by the Council.

However, Mr Thomson, speaking no doubt on behalf of the second defendant rather than the first, submitted that by reason of the events that have occurred there is no fund upon which a charge can attach. This submission follows from the liquidators' abandonment of the contract and the Council's assertion that the cost of completion of the works by another contractor exceeded the unpaid balance of the contract sum under the Newbury contract. (J.J. Craig Ltd v Gillman Packaging Ltd /1962/ NZLR 201).

Clause 19.1 of the General Conditions provides for the event of abandonment, and as I have said entitles the principal to take possession of the works or determine the contract. Seven days' written notice of the principal's intention must be given to the contractor. The contractor's right to payment depends on the course the principal adopts. If he determines the contract, the contractor is entitled to no more than he has already been paid. If the principal elects to take possession of the works, the contractor is entitled to the value of work completed, subject to set off to the extent that the total cost of completion exceeds the contract price. In this case, it does not appear that the Council gave the notice contemplated by cl.19.1. The evidence given by its quantity surveyor shows that nonetheless it took the steps appropriate to having taken possession of the works. The work done up to abandonment was valued, and the final calculations made by the quantity surveyor assume that Newbury is entitled to be credited for the work done during the currency of the contract, including that done by South Pacific, but is to be debited with the final cost of completion.

Whilst the result of abandonment by the contractor of a contract such as this is that no further moneys are payable to the contractor, and subcontractors' rights to a lien or charge are limited to such retention moneys on progress payments already made as are not absorbed in the cost of completion (Ashby Bergh & Co Ltd v Ross Borough

/1972/ NZLR 1069), I am not satisfied that that is the result which follows in this case. This contract differs from that in the Ashby Bergh case, in that in the latter only one remedy was provided, namely for the principal to take possession of the works upon notice. The principal did not exercise that right and was therefore treated as having independently of the terms of the contract accepted the contractor's repudiation. In the present case, the choice between the two remedies is provided by the contract itself. Although the formal notice whereby the choice is to be exercised was not given, it is clear that Newbury waived the necessity for it, for it gave notice of abandonment itself, and it now appears to support the Council's attitude in these proceedings. It is also clear that the Council, again with Newbury's tacit support, has adopted the course of taking possession. Having done that, the Council is in my view required to draw up its accounts with the contractor on that basis.

The point is probably only of academic interest, for the likelihood is that there is no fund to charge. If there is, then South Pacific's rights under the Act depend upon its compliance with the statutory conditions, and in particular upon the giving of notice in terms of s 26(2) of the Wages Protection and Contractors Liens Act within 30 days of "the completion or abandonment of the work in respect of which it is claimed." If there are funds, compliance with this time limit is essential to South Pacific's ability to share in them, for if it was out of time its claim will be relegated in priority behind other claims which I understand will more than absorb all that is likely to be available.

South Pacific's notice of claim was dated 18 November 1977 and was served that day. It refers to work "done by the sub-contractor between the 19th day of September 1977 and the 18th day of October 1977."

The latter date appears to have been the last day on which South Pacific worked on the job. If that is to be regarded as the date of completion of South Pacific's work the notice appears to have been given out of time, for a 30 day period from 18 October would have expired on 17 November. However, if South Pacific is properly to be regarded as having abandoned the work, then that may not have occurred until the following day, and consequently the notice will have been given in time. This topic was not fully canvassed. Argument at the hearing centred on the questions of novation and assignment rather than on the issues that follow from the resolution of those questions. As I am unable in any event to conclude the matter by this judgment, I propose to reserve leave to the parties to make further submissions on this aspect of the case should they consider that necessary.

Finally, and briefly, I make some tentative comments on the other issue which must be decided to bring the matter to finality, namely the rights of South Pacific in the liquidation of Newbury. The question is simply whether the liquidators are entitled to disclaim any responsibility towards South Pacific. As I have already pointed out, the Official Assignee contracted with South Pacific pursuant to the powers conferred on him by s 240 (1)(b) of the Companies Act. To protect himself, he took indemnities from the major creditors. That was a necessary precaution, in case for example there was at the end of the day insufficient to meet the costs incurred. In those circumstances, the Official Assignee as provisional liquidator might himself have been liable to those with whom he had contracted on the company's behalf (cf Brown v Cowan (1912) 31 NZLR 1219). Short of that situation, the rights of a creditor whose debt has been incurred as a result of the liquidator carrying on the business are clear. They were expressed thus by Fry LJ in In re International Marine Hydropathic Co (1884) 28 Ch 470, 473:

> "If the debt or liability is incurred by the liquidator or by the company after the winding-up, in the course of carrying on the business of the company, it must be paid in full. Such debts and liabilities are not debts and liabilities of the company in liquidation. They are debts and liabilities incurred subsequently to the liquidation, and it seems monstrous that the company should be allowed to carry on its business for its own purposes without paying the debts which have been incurred by so carrying it on."

The law is not monstrous. In In re Great Eastern Electric Co [1941] 1 Ch 241, Simonds J said at p. 244:

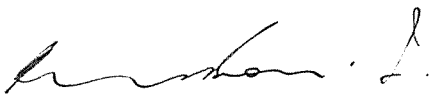
> "If in the proper exercise of this statutory power he incurs obligations, those to whom he incurs them are entitled to be paid out of the assets of the company in priority to its creditors at the commencement of the winding up. It cannot, in my judgment, make any difference whether the obligation be in respect of rent or rates or goods, if it is incurred in the due course of winding up and the condition is satisfied that the continuance of the business is necessary for the beneficial winding up: see In re National Arms and Ammunition Co (1885) 28 Ch D 474, 481 and particularly the judgment of Bowen L.J. The test will be the same whether, as is the more usual case, the liquidator, having discharged the obligation, claims to be allowed it in his accounts, or, as here, the post-liquidation creditors, not having been paid, claim to rank in front of the pre-liquidation creditors. There can be no question of the two classes ranking pari passu: if the condition is satisfied the post-liquidation creditors come first; if not, they do not come in at all - at any rate until the pre-liquidation creditors have been satisfied."

The pre-condition to preferential payment referred to in this passage is not in question in the present case. If it was, it might be another instance covered by the prudent step the Official Assignee took to obtain indemnities. As matters stand, the position seems to have been properly

expressed by Mr Jobberns in the passage I have quoted from his letter to the Council on page 3 of this judgment.

The rights of the parties are of course also regulated by s 261 of the Companies Act which provides that where the assets are insufficient to satisfy the liabilities, the Court may make an order as to the priority in which costs, charges and expenses incurred in the winding-up are to be paid. There is no application under this section before me and indeed I am not in the position of making any final determination on the point because it was not fully argued and the Official Assignee was not represented at all. It nonetheless seemed that it may be helpful if the relevant principles were to be mentioned at this stage: for not only are they clear, but it seems to me as I am at present advised, that the fact that the Official Assignee has been replaced by the liquidators is immaterial to the rights of South Pacific in the liquidation.

This I think is as far as I can take the matter at present. If further matters require my determination, then Counsel should inform the Registrar whether they are content to refer them to me in writing, or whether they wish arrangements to be made for the hearing to be resumed.



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