N.Z. Wines v. Commercial Realties

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IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY

(Land)

A 413/82

BETWEEN NEW ZEALAND WINES AND SPIRITS (PROPERTIES) LIMITE

First Plaintiff

A N D NEW ZEALAND WINES AND SPIRITS LIMITED

Second Plaintiff

A N D COMMERCIAL REALTIES (NZ) LIMITED

Defendant



A 139/83

BETWEEN COMMERCIAL REALTIES (NZ) LIMITED

Plaintiff

A N D NEW ZEALAND WINES & SPIRITS (PROPERTIES) LIMITED

Defendant

Hearing: 15 and 16 May 1984

Counsel: A.H. Brown for New Zealand Wines & Spirits (Properties) Ltd and New Zealand Wines & Spirits Ltd
R. Chapman for Commercial Realties (NZ) Ltd

Judgment: 23/5/84

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JUDGMENT AND REASONS FOR JUDGMENT OF SAVAGE J.

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In this case two actions were heard together by consent of the parties. It was clear, as will become apparent later in this judgment, that a determination of one action would

necessarily determine the other. The dispute between the parties arose out of a contract for sale and purchase of land. New Zealand Wines and Spirits (Properties) Ltd, the first plaintiff, owned a property, being a little over an acre in area, situated at 3-23 Hutt Road, Wellington. This company is a property owning company. New Zealand Wines and Spirits Ltd, the second plaintiff, was referred to as the parent company of the first plaintiff and it carries on a wine and spirit business. The defendant carries on business as a property owning company. On or about the 11th August 1982 the first plaintiff and the defendant entered into an agreement in writing for the sale and purchase of the Hutt Road property. The sale price was $950,000. The deposit paid by the defendant as purchaser was $10,000. One of the terms of the agreement was that the purchase price was subject to a vendor's mortgage of $800,000, to be secured by a first mortgage over the land, and it followed that the amount of cash payable in respect of the purchase price on settlement was $140,000.

The property was leased to five separate tenants under formal leases for lengthy periods and all the leases contained rights of renewal for varying terms. In addition to the five leases part of the property was occupied by a liquor business run by the second plaintiff. The agreement for sale and purchase provided that the parties would enter into a deed of lease whereby the first plaintiff would take a lease back of a specified portion of the property on terms and conditions nominated in the agreement. In fact it appears that later the

parties agreed that the lease back should be to the second plaintiff, not the first plaintiff, but in the event this point is of no importance to the issue before the court, though it explains why the second plaintiff was joined in the proceedings. A clause of the agreement, clause 12.3, upon which the issue in this case depends, provided that the agreement was conditional upon "the purchaser's solicitors approving the titles to the property and lease documents within a period of 21 days from the date of acceptance hereof". It should be recorded at this point that the five existing lessees of the property were all private companies. Subsequently the defendant's solicitors, as solicitors to the purchasers, raised with the plaintiffs' solicitors, as solicitors to the vendor, various matters in relation to the transaction. It is not necessary to canvass these, save in respect of the matter of the leases. A director of the defendant, a Mr J.W.K. Urlich, had been supplied, prior to the agreement for sale and purchase being completed, with copies of the leases or at all events with four out of the five. These had been handed on to the defendant's solicitors and they, after the agreement was signed, asked the plaintiffs' solicitors for a copy of the fifth lease and also for a draft lease in respect of the premises that were to be leased back to the vendor for perusal. The agreement for sale and purchase had expressly provided that the lease was to be prepared by the vendor's solicitors and was to contain certain specified terms and "all other usual terms". The fifth lease was provided as requested,

as also was the draft lease, for perusal. The defendant's solicitors then wrote to the plaintiffs' solicitors and expressed concern at the lack of personal covenants in all the five existing leases. The solicitors said it was customary for personal covenants to be obtained particularly where the lessee was a private company, and they regarded the matter as of critical importance. They went on to say that it was presumably impossible at that point "to obtain personal covenants from the shareholders/directors of the various lessees" and they therefore asked that the first plaintiff agree either to guarantee the existing leases or to enter into a deed agreeing to take over the existing leases in the event of any of them being determined for breach by the lessee prior to the expiry of the existing terms or any renewals. The solicitors then went on in their letter to deal with various points in the draft lease submitted for perusal which they wished to have amended but, though it made no provision for a personal covenant guaranteeing performance to be executed by any shareholders or directors, they did not require one to be inserted. The first plaintiff's solicitors, while accepting the amendments proposed, advised that the first plaintiff was not prepared to guarantee the existing leases. The defendant's solicitors thereupon replied that in view of the absence of personal guarantees they were unable to approve the leases in terms of the contract and accordingly the contract was at an end. They asked the plaintiffs' solicitors to authorise the agents to return the deposit to them. The plaintiffs declined

to do so and called on the defendant to complete the contract, contending that the reason given by the defendant's solicitors for refusing to give their approval was not one that they could properly take into account in terms of the clause in the contract. The defendant then commenced proceedings in the District Court at Wellington claiming the return of the $10,000 paid by way of deposit. The first plaintiff filed a defence and issued these proceedings claiming a decree of specific performance and judgment for various sums of money, being the $140,000 balance purchase price, interest, and certain other sums that would be due in terms of the agreement. The proceedings in the District Court were removed into this Court and, as noted earlier, the two actions are being heard together.

Various issues were raised on the pleadings but both counsel agreed that the sole issue before the Court is whether the ground given by the defendant's solicitors for refusing approval to the agreement for sale and purchase in terms of clause 12.3 was justified. In short the issue is whether it was permissible to decline approval for the reason that the existing five leases did not contain personal guarantees nor were such guarantees otherwise given by means of a separate deed of covenant.

When the hearing commenced, Mr Brown advised me that the agreement for sale and purchase had not been stamped. He drew my attention to s 69(1) of the Stamp and Cheque Duties Act 1971 which declares that an unstamped instrument shall not be admissible in evidence and subsection (2) which requires the

Court to take note of the fact that an instrument is not stamped. Provision is made in subsections (2) and (3) for the payment into court of the duty and the submission of the instrument and the duty to the Inland Revenue Department. Mr Brown then formally tendered the duty and the agreement for sale and purchase, both of which were forwarded to the Department, and the agreement was duly stamped.

Stated briefly, the plaintiffs' case, and the way I now express it is not precisely the way counsel put it, was that a binding agreement had been entered into by the parties subject to a condition subsequent contained in clause 12.3; that clause had to be construed by reference to the intention of the parties and in the context of the particular agreement; in this case it was to be construed as meaning that the solicitors' approval was limited to the conveyancing aspects of the contract and did not include the commercial or value aspects of the bargain; the solicitors' refusal of approval was for a reason that related to the commercial or value aspects of the bargain and not to the conveyancing aspects, for what the defendant sought was additional security which was a matter that went to the value of the bargain and was not concerned with the conveyancing aspects of the bargain actually reached. The defendant, on the other hand, accepted that a contract was formed, subject to a condition subsequent, and that it should be construed having regard to the commercial purpose of the contract and the factual background against which it had been made but submitted that the solicitors' refusal to approve the

agreement was a proper exercise of the solicitors' function in terms of the clause. The solicitors' refusal was motivated not chiefly by the commercial side of the bargain but because personal covenants by shareholder directors were a usual part of lease documents and their absence meant the lessor would lack a remedy he ought to have. Both counsel relied upon the judgments in the Court of Appeal in Provost Developments Ltd v Collingwood Towers Ltd [1980] 2 NZLR 205. In that case there was an agreement for sale and purchase which included a clause which read "subject to solicitors approval by Friday 30th June 1978 by 5 p.m.". The relevant part of the headnote to the case reads:

> "The natural interpretation of clause 19 was that the parties had struck a bargain which was to be honoured unless some legal pitfall was discovered by the solicitors. They were to consider, not all the terms and conditions from the point of view of mere expediency in the interests of their clients, but the conveyancing aspects of the transaction, using those words in a liberal sense to include legal impediments and implications."

Both counsel, in developing their arguments, relied on some observations of Lord Wilberforce in Reardon Smith Line Ltd v Hansen-Tangen [1976] 3 All ER 570. I refer to three passages. First at p 574:

> "It is less easy to define what evidence may be used in order to enable a term to be construed. To argue that practices adopted in the shipbuilding industry in Japan, for example as to sub-contracting, are relevant

> in the interpretation of a charterparty contract between two foreign shipping companies, whether or not these practices are known to the parties, is in my opinion to exceed what is permissible. But it does not follow that, renouncing this evidence, one must be confined within the four corners of the document. No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what is legitimate to have regard to is usually described as 'the surrounding circumstances' but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating."

Second, also at p 574:

> "It is often said that, in order to be admissible in aid of construction, these extrinsic facts must be within the knowledge of both parties to the contract, but this requirement should not be stated in too narrow a sense. When one speaks of the intention of the parties to the contract, one is speaking objectively - the parties cannot themselves give direct evidence of what their intention was - and what must be ascertained is what is to be taken as the intention which reasonable people would have had if placed in the situation of the parties. Similarly, when one is speaking of aim, or object, or commercial purpose, one is speaking objectively of what reasonable persons would have in mind in the situation of the parties."

Third and lastly at p 575:

> "I think that all of their Lordships are saying, in different words, the same thing – what the court must do must be to place itself in thought in the same factual matrix as that in which the parties were. All of these opinions seem to me implicitly to recognise that, in the search for the relevant background, there may be facts, which form part of the circumstances in which the parties contract, in which one or both may take no particular interest, their minds being addressed to or concentrated on other facts, so that if asked they would assert that they did not have these facts in the forefront of their mind, but that will not prevent those facts from forming part of an objective setting in which the contract is to be construed."

Mr Chapman submitted that the background in this case was that Mr Urlich, who on behalf of the defendant had conducted many of the negotiations with the plaintiff, was on the evidence a person inexperienced in the purchase of commercial property and thus felt he and the other director needed the advice of their solicitor to protect their position in regard to legal matters that related to the purchase of the property and it was for that reason that the solicitors' approval clause to deal with leases and related matters was included in the agreement. Further, he submitted, it was a complex transaction involving long leases and a condition subsequent in the contract on which the defendant would need legal advice. I do not think the intention of Mr Urlich attributable to his inexperience in this

kind of commercial property purchase transaction as given by him in evidence is a background fact to this transaction which can be taken into account. I think Mr Brown was right when he submitted that the evidence of Mr Urlich's intention was impermissible. I think the background facts must be viewed, as Lord Wilberforce said in the passages cited earlier, in an objective way. So far as the other factor to which Mr Chapman referred is concerned, I would observe that in fact Mr Cain, the defendant's solicitor, was consulted by Mr Urlich well before the agreement was signed on the 11th August. Indeed, some of the clauses in the agreement were amended on his advice before it was signed on the 11th August.

Mr Chapman had submitted that it is not easy to define the precise limits of a solicitor's function under a clause such as the one in this contract. The question, as he submitted, and as is clearly stated in the Provost case, is a question of construction. In the words of Richardson J. in that case at p 212 it is a matter of arriving at the true intention of the parties as expressed in the instrument considered against the surrounding circumstances as they existed at the time of its execution. No general principle can be laid down and each case must be considered separately, but at the same time, the views of the Court of Appeal on a similar though apparently considerably wider clause as to the role of solicitors is obviously of assistance. Mr Chapman, at all events, accepted that the solicitors' function under this clause was limited to the area of what might reasonably be expected of a conveyancing

solicitor in the light of all the circumstances. He submitted that what might be expected of a conveyancing solicitor might vary according to the kind of persons who were parties to the agreement or the kind of property the subject of the agreement. I think this submission is correct but I do not think it helps the defendant in this case. The position must be viewed in an objective sense on the basis of what reasonable persons would have intended if placed in the situation of the parties. See Reardon Smith Line Ltd v Hansen-Tangen (supra) at p 574h. I do not think there is anything in the evidence which would have suggested the parties had in mind any special or particular function for the defendant's solicitor in relation to the defendant as a company or its directors as persons. I accept that the solicitors' function might well vary according to whether the property involved was a million dollar building, as here, or a small fish and chip business. I do not think, however, that this point has any special relevance in this case.

There was some difference of opinion in the evidence of Mr Cain, as solicitor for the defendant, and Mr Goodwin, as solicitor for the plaintiff, in respect of conveyancing practice on the question of the giving of personal covenants by shareholders and directors of private companies on the granting of leases to the companies. Mr Cain expressed the view that such personal covenants were almost invariably required, at least in Wellington; Mr Goodwin, on the other hand, thought it was not uncommon for them to be required but that it really depended upon the standing of the tenant. It is not necessary

for me to determine this question, because I have reached the conclusion it is not a matter which comes in this case within the solicitors' function as envisaged by the clause in the agreement.

In my view, the solicitors' function was restricted to what might reasonably be expected of a conveyancing solicitor in relation to the agreement before him, which was the agreement for sale and purchase. In terms of that agreement the defendant was purchasing the property subject to the existing leases. The agreement contained other provisions including provisions for a mortgage and a lease back to the vendor. The solicitors' function was in relation to that contract. Had the solicitors been concerned as solicitors for a lessor in respect of an agreement which included the granting of leases to the private companies, then no doubt the question of personal covenants by the shareholders and directors of the lessees would have come within the scope of the solicitors' function. Indeed, in this very transaction that aspect arose as the solicitors for the defendant were concerned to consider the lease back to the plaintiff, which is a private company, and it is not without significance on the question of such personal covenants being required in a conveyancing sense that the solicitors had not sought them from the shareholders and directors of it when they approved the draft lease which had been submitted. That issue, however, is not really relevant here, where the question is the scope of the solicitors' function in relation to the agreement for sale and purchase

between the first plaintiff and the defendant and is not concerned with an agreement to lease involving the original lessors and the lessees of the existing five leases.

The situation of the parties when this agreement was entered into on the 11th August was that the parties had been negotiating over the transaction for some weeks before the agreement was executed. The defendant had had full details of the property, having been supplied with various reports and valuations, and the existing leases. The defendant knew precisely what it was buying and the terms of the purchase had clearly been very carefully considered, for there were to be both a mortgage back and a lease back. The defendant was well aware that under the existing leases the rents were to be reviewed within a relatively short time and it expected substantial increases. The function of the solicitors to the defendant in those circumstances was, in my view, no more than that of the solicitors in the Provost case. It was to consider the conveyancing aspects of the transaction between vendor and purchaser, including all legal impediments and implications, but it did not include the elements and merits of the bargain that had been reached. Here the defendant had agreed to purchase the property subject to the existing leases; that was the bargain. The reason given for refusing approval was, in my view, essentially that one of the elements of the bargain was not worth as much as the solicitors considered it should have been, and would have been, if at the time the leases had been entered into by the lessor and the lessees personal covenants

had been given. At that time the matter of personal covenants might well have been a conveyancing matter in relation to the leases to be executed but at the stage this agreement was executed the leases, without personal covenants, had long since been executed and were in that form part of the property being purchased by the defendant from the plaintiff at an agreed price. To raise the question of personal covenants in relation to them was not to deal with a conveyancing matter relating to the contract for sale and purchase but was to attempt to increase the value of the property the subject matter of the sale. In result I am satisfied that the solicitors' refusal of approval was not within the scope of the clause in the contract and accordingly is ineffective. I should add, however, that it may well be that had some issue as to the legal validity of the existing leases been raised, or some question as to their form in a conveyancing sense, then that question might well have come within the scope of the solicitors' function in terms of the clause.

It follows that the plaintiffs are entitled to succeed in their action. There will therefore be an order for specific performance of the contract and for judgment in respect of the other claims set out in the amended prayer for relief. I understood Mr Chapman to accept that the plaintiff was entitled to relief in accordance with the amended prayer for relief but if he wishes to be heard further upon it leave is reserved to the defendant to apply. The plaintiffs are entitled to costs in their action. If the parties are unable to agree upon the

costs, leave is reserved to both to apply for further directions. This result means that the second action, in which the defendant, Commercial Realties Ltd, was plaintiff, fails and New Zealand Wines and Spirits (Properties) Ltd as defendant is entitled to judgment. I do not allow costs in that action, however, other than for disbursements.

Solicitors for first and second plaintiffs: Russell, McVeagh, McKenzie, Bartleet & Co. (Auckland)

Solicitors for defendant: Roache, Cain & Chapman (Wellington)