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IN THE HIGH COURT OF NEW ZEALAND 12/3
AUCKLAND REGISTRY

CP 1062/91

BETWEEN DOWNSVIEW NOMINEES LIMITED

Plaintiff

LOW PRIORITY

163

A N D JOHN TUCK and FREDERICK WATSON of Auckland, Chartered Accountants as the liquidators of REGISTERED SECURITIES LIMITED

Defendants

Hearing: 2,3 February 1993

Counsel: Ms M J McCartney for Plaintiff
A K Singh and Miss Chamberlain for Defendants

Judgment: ~~2nd~~ 16th February 1993

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# JUDGMENT OF SMELLIE J

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## INTRODUCTION

A company named Maughold Enterprises Ltd (MEL), having acquired land in the Bay of Islands established upon it a motel. As part of the financing for the enterprise and the fitting out of the motel MEL borrowed moneys from Registered Securities Limited (RSL) secured in part by way of a floating charge. Subsequently MEL also borrowed moneys from Downsview Nominees Limited, the Plaintiff, (DNL) which company took an instrument by way of security over certain chattels. The case concerns a dispute between RSL (now in liquidation) and DNL as to which charge over the chattels in the motel has priority.

## THE ESSENTIAL FACTS

RSL's debenture was executed on 30th September 1986 and registered on 2nd October 1986. By clause 2 of the same MEL charged in favour of RSL all the company's undertaking and all its property and assets. By clause 3 of the debenture the charge was said to be a floating charge only but specifically provided that "... the company shall not be at liberty without the consent of the mortgagee to create any further mortgage or charge upon the property and assets comprised in this security to rank either in priority to or pari passu with the charge hereby created ...".

DNL made advances to MEL in 1985 and 1986 and a further advance of $100,000 in 1987. When the last advance was made DNL took an instrument by way of security from MEL which was dated 5th April 1987 and registered on 27th April 1987.

RSL's floating charge also provided, pursuant to clause 19 of the same that it would crystallise, inter alia, if a receiver was appointed or an encumbrancer took possession. RSL appointed receivers on 30th September 1988 and went into possession late October, early November 1988.

Other essential facts were in dispute between the parties and will be dealt with later in the judgment.

## THE BASIS OF THE PLAINTIFF'S CLAIM FOR PRIORITY

The Plaintiff claims that its charge has priority in respect of the chattels on two grounds. First it says that RSL consented to MEL giving it a first charge over the chattels. Secondly it says that $2,200,000 which RSL advanced to MEL up to and including 30th April 1987 was repaid and then readvanced to MEL on or about 8th April 1988. On that basis the Plaintiff says that the rule in ***Hopkinson v Rolt*** operates in its favour to give it priority.

## THE DEFENCE

The Defendants say that as a matter of fact consent was never given and further as a matter of fact the $2,200,000 was never repaid and was still owing as originally advanced when the floating charge crystallised and as a consequence the rule in ***Hopkinson v Rolt*** has no application.

## DID RSL CONSENT TO DNL'S CHARGE

It was common ground that because of the provisions of s4(2) of the Chattels Transfer Act 1924 DNL had notice of the provisions of clause 3 of the debenture once it was registered.

No witness was called to say that either written or oral consent was ever given. Nor was any document produced to that effect. Mr C L Samuel, presently serving a term of imprisonment for perjury, who had formally been a Director of RSL, was called to give evidence and said specifically that he could not recall whether or not any request had been made for consent or whether such consent had been given. Miss McCartney submitted, however, that the Court should draw the inference that consent had been given from the surrounding circumstances in the case. Counsel pointed out that the wording of clause 3 in the debenture simply refers to "without the consent of the mortgagee". Unlike, for example, the provision in the well known case of ***Re Manurewa Transport Ltd*** [1971] NZLR 909 where the wording was "prior written consent". She submitted that the fact that at a later stage on 8th April 1988 when RSL made further advances to MEL it took an instrument by way of security over the same chattels that were secured by DNL's instrument shows that RSL accepted that by then DNL was the first charge holder. Counsel submitted that the only explanation for the taking of the instrument by way of security by RSL at the later stage was because the Plaintiff had priority.

In addition Counsel submitted that the terms of a letter written by the solicitors acting for the Defendants on 25th September 1990 was further evidence that DNL did in fact have a first charge. The fourth paragraph of the letter which is document 342 in the agreed bundle of documents reads:-

> "Our inquiries reveal that the Downsview Nominees' instrument was meant to have been repaid as one of the conditions for the advance made by RSL under its instrument by way of security. We are of the impression that this had been done, however note that no satisfaction has been registered at the Companies Office."

Counsel's submission was that the requirement that DNL's charge should be repaid before further advances were made "would not have been

necessary but for RSL's acceptance that consent had been given to the DNL instrument by way of security as a first charge."

I am not persuaded by the evidence relied upon that it would be proper to draw the inference Miss McCartney urged upon the Court. Both the taking of the subsequent instrument and the apparent requirement that was not carried through that out of the further advances DNL's instrument should be discharged, do not point in my judgment convincingly to consent having been given. To my mind the fact that at the relevant time RSL was increasing its overall lending and security from $2,200,000 to $4,500,000, provides a perfectly adequate and acceptable explanation for the mortgagee's requirement that the limited lending ($190,000) to DNL should be cleared away and maximum security, including an instrument by way of security, should be taken.

I therefore hold as a matter of fact that consent was not given orally or in writing at any stage.

## WAS THE $2,200,000 REPAID AND READVANCED?

It was again common ground between Counsel that the rule in ***Hopkinson v Rolt*** (1861) 9 HL Cas 514, provides that priority will not apply in respect of moneys advanced after moneys are advanced by a second charge holder, if the first charge holder has actual knowledge of the existence of the later charge at the time of the further advances.

It follows that the Plaintiff can only take advantage of the rule if it can show that the $2,200,000 was repaid and that the total borrowings of $4,500,000 were all advanced in April of 1988 which was after the date of advance of the DNL money. For the purposes of this part of the case I take it as accepted by the Defendants that as at April 1988 RSL was aware of the DNL advances. That seems to be supported by the terms of letter no 342 referred to earlier.

The real contest between the parties therefore was whether or not there had been a complete repayment of the original advance of $2,200,000 followed by a readvance of those same moneys together with others leading to the $4,500,000 odd loan secured by both mortgage and instrument by way of security.

On this issue Mr Samuel gave evidence that he had negotiated certain advances on behalf of RSL to MEL and that it was his intention at the time of negotiating those advances that if further moneys were to be loaned the $2,200,000 should be repaid. Mr Samuel acknowledged that he was not in control of or au fait with the day to day accounting records of RSL but his evidence was that the fact that the accounting records do not show a repayment of the $2,200,000 and a readvance of that amount along with the other moneys in April of 1988, did not surprise him because he said he had found in the past that the financial records of RSL were not always reliable.

The documents registered in the Land Transfer Office at the time of the alleged readvance in April of 1988 recorded that the $2,200,000 had not been repaid in that the Memorandum by way of Variation of Mortgage, registered on 3rd May 1988, contained in para 30 of the same, under the heading "Mortgage by way of Variation" the following provision:-

> "30. This mortgage secures in part the full principal sum under mortgage B604302.7 and is intended to operate by way of variation of mortgage B604302.7."

It was common ground that the last mentioned mortgage was the one which had been registered on 26th November 1986 to secure the original advance and then subsequently varied on 18th March 1987 when the full $2,200,000 had been advanced. Mr Samuel maintained, however, that that was not what was intended and not what happened.

The Defendants called Jacqueline Lee Sibbald, a partner in the firm of Keegan Alexander Tedcastle & Friedlander, Solicitors of Auckland, who acted for RSL in respect of its advances to MEL over the relevant periods in 1986, 1987 and 1988. Miss Sibbald's evidence was that she prepared the Memorandum of Variation of Mortgage and instrument by way of security which secured the total advances of $4,500,000 odd on instructions she received from RSL. She was adamant that the $2,200,000 had not been repaid and that clause 30 of the Memorandum of Variation of Mortgage set out above was inserted specifically because the original advance was not being repaid and the additional advances were to be secured in part by way of variation of the original mortgage. Miss Sibbald also gave evidence that

she had checked the trust ledger of her firm and it showed that there had been no movement through the ledger of $2,200,000 as part of an overall advance of $4,500,000.

In her submissions to me Miss McCartney submitted that Miss Sibbald's evidence should not be accepted and that it was not possible to have a mortgage such as the one registered in May of 1988 which purported to vary an earlier mortgage whilst at the same time securing further advances and leaving that earlier mortgage still on the title. It may be that the procedure adopted by Miss Sibbald is not much employed by conveyancers generally. Having considered the matter, however, including the further submissions in writing filed by Counsel pursuant to leave given, I am not persuaded that the way things were done on this occasion is any reason for me to doubt the truth and reliability of the evidence given by Miss Sibbald.

In addition to the solicitor's evidence the Defendants called Mr Ian McLennan, an accountant employed in the liquidation of RSL. His evidence was that it was part of his job to become familiar with the accounting practices of RSL before it went into liquidation. He said in para 5 and following of his prepared brief:-

> "5 I have found that the accounting system of RSL is different from most other accounting systems because it deals on a cash basis. It is totally driven by the receipts of cash and the payments of cash. It does not run on an accruals basis which deals in invoices produced and invoices received. It relies on cash books and entries which appear on bank statements.
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> 6. In that regard, RSL's records are therefore complete and accurate as recorded in the cash books and entered in the general ledger, the mortgage ledger and the investors ledger.
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> 7. It is not unusual for large businesses to use such an accounting system, but it was necessary for RSL to do so because RSL was a nominee company and was working in a trust environment.
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> 8. I have not discovered any weaknesses in the cash-recording system of RSL and have no reason to believe that RSL's cash-recording

> system produced any inaccuracies. The auditors of RSL also have not found any problems with the cash recording system of RSL. The system is actually easier to follow and to check the accuracy of than an invoice based accrual system."

Mr McLennan went on to record in his evidence in chief that the records of RSL do not show a repayment and readvance of the $2,200,000 as alleged by the Plaintiffs. This witness was of course cross-examined by Miss McCartney and challenged as to the reliability of the conclusion he had reached that there was no repayment and readvance. At the end of it all, however, I was left satisfied that Mr McLennan was a careful, intelligent, reliable witness whose evidence I could accept.

I find as a fact that the $2,200,000 was not repaid and readvanced. It follows that the priority that RSL had prior to the advances by DNL was not lost and RSL was as a consequence entitled as first charge holder to take possession of the chattels once the receivers were appointed.

## CONCLUSION, ORDER AND COSTS

Having reached the conclusion that RSL maintained priority for its charge throughout, I need not address the question of value of the chattels (although that was agreed between Counsel during the course of the trial) or the issue of the alleged conversion of the same.

It is appropriate that I formally order that the $150,000 plus interest earned on that sum, deposited by the Defendants pursuant to the order of Anderson J on 18th July 1991 when interim relief was applied for by the Plaintiffs, should now be paid out to the Defendants.

The Defendants are also entitled to costs which I fix in the sum of $1,500, plus filing fees and disbursements as fixed by the Registrar.

Robert Smellie J

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Solicitors

Bell Gully Buddle Weir for Defendants
Cairns Slane for Plaintiff