CA218

LOW PRIORITY

IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

20/5

CP.7/94

615

BETWEEN	EVERARD FILMS DISTRIBUTORS LIMITED	
	Plaintiff	
AND	SBSA (NZ) LIMITED	
	Defendant	
AND		CP.168/94
BETWEEN	SBSA (NZ) LIMITED	
	Plaintiff	
AND	EVERARD FILMS DISTRIBUTORS LIMITED	
	Defendant	

Hearing: 9 and 10 May 1994

Counsel: N. W. Ingram and W. Brandon for Plaintiff in CP7/94 and Defendant in CP168/94
P. Davison and F. E. Baker for Defendant in CP7/94 and Plaintiff in CP168/94

Judgment: 17 MAY 1994

JUDGMENT OF BLANCHARD, J.

Solicitors: JRB Kingston & Co., Auckland for Plaintiff in CP7/94 and Defendant in CP168/94
Rudd Watts & Stone, Auckland for Defendant in CP7/94 and Plaintiff in CP168/94

SBSA (NZ) Limited ("SBSA"), a subsidiary of State Bank of South Australia, is the mortgagee in possession of a theatre complex in Queen Street, Auckland known as the St James Theatre Centre. It consists of four movie theatres and their ancillary areas, with which this litigation is concerned, and some retail shops. Title to the St James Theatre Centre is vested in Kerridge Odeon Corporation Ltd from whom SBSA holds a mortgage. Until the beginning of 1993 the cinemas were operated by another company in the Pacer Kerridge Group known as Pacer Kerridge Cinemas Ltd and the portions of the ancillary area used for sale of ice creams and confectionary were operated by another company in that group called Nibble Nook Ltd. Because of the financial problems being experienced by Pacer Kerridge Group the complex has been in a run down condition. It has also increasingly suffered from competition from new multiplex cinemas established on the North Shore at Wairau Park (opening in May 1992) and Newmarket (opening in the latter part of 1993).

When Kerridge Odeon Corporation fell into arrears with its payments due under the mortgage SBSA at first appointed Mr John Rofe, insolvency practitioner of Arthur Anderson in Auckland, as receiver of rents. That occurred early in 1991. Then on 20 August 1991 SBSA took steps to go into possession by directing that rents be paid to Mr Rofe as its agent. From at least August 1992 onwards Everard Film Distributors Limited ("Everard") a company owned and controlled by Mr Barrie Everard became interested in the possibility of involving itself in operation, refurbishment, and possibly ownership as well, of the complex. In conjunction with Endeavour Services Corporation Everard put a proposal for a seven year lease to Mr Rofe in August 1992. Everard and Endeavour contemplated jointly purchasing all of the Pacer Kerridge Cinema businesses throughout New Zealand. They

believed that the St James complex required capital expenditure of at least $1m to bring it up to an acceptable modern day standard and they naturally were looking for security of tenure for as long a period as possible. Seven years is the maximum term for which a mortgagee in possession may lease the mortgage property: s.91 Property Law Act 1952. Nothing came of the proposal but Everard remained interested.

By Christmas 1992 the financial position of Pacer Kerridge Cinemas Ltd had evidently worsened and receivers were appointed by the syndicate of banks which held securities over that company. SBSA was one of those banks. The receivers were partners in Ferrier Hodgson & Co.

On 7 January 1993 there was a meeting between Mr Rofe and Mr Everard. It is common ground that Mr Everard was looking to obtain a lease of the cinema complex for his company for a six month period for evaluation of trading performance of the cinemas and a further six months to plan future development. The opening of the Wairau Park multiplex had already impacted but there had been some delays on the Newmarket project and it was now not expected to open for business until about August 1993. So its impact would not be able to be measured until then.

The position of SBSA and its agent was one of some difficulty. There were arrears in the payments due from Pacer Kerridge Cinemas Ltd and Nibble Nook Ltd and a substantial amount of rates had not been paid. Because of the run down state of the complex and the insolvency of the cinema operator and also because of the generally depressed state of the Auckland property market it was not going to be easy to find a buyer for the complex at a figure acceptable to SBSA. One possibility was sale to someone like Everard which would itself operate the cinema business.

Another possibility, if a stable long term tenant could be found paying a market rent, was for sale to a property investor. But obviously an investor would be discouraged if there was no stable long term lease. For understandable reasons Everard, which had limited financial resources, was adopting a cautious approach. In January 1993 it was not offering to take up a long term lease nor to purchase the complex. But even if it obtained only a short term lease the possibility of an immediate sale to an investor would diminish.

Having received an indication from Mr Rofe that a short term lease of some kind might be available Mr Everard busied himself in negotiations with the receivers of Pacer Kerridge Cinemas and by 19 January he was in a position to make a conditional offer for the purchase of the business of Pacer Kerridge Cinemas. The offer encompassed cinema operations at another site in Auckland and at sites in Wellington, Christchurch and Dunedin as well as the St James Centre. The offer was open for acceptance only until 9.00 a.m. on 20 January. By that time he had received an indication that the offer was acceptable, subject to negotiation of final documentation. An agreement with the receivers was signed on 22 January.

In the meantime Mr Everard had gone back to Mr Rofe, with whom he had had some further discussions since 7 January.

On 20 January Mr Rofe prepared a draft letter to Everard Films Ltd referring to discussions of "today's date" and noting the terms under which Everard wished to lease the St James Theatre Centre. He referred to a rental of $200,000 and a term "for a period of 12 months". In the paragraph of the letter referring to the term Mr Rofe stated:

> *"We understand this will provide you with an opportunity to assess the viability of developing the property into a six screen multiplex. Prior to one month before the expiration of the initial term you would notify the Mortgagee in writing of your intention to enter into a further period of lease on terms acceptable to both yourselves and the Mortgagee."*

It is the meaning of the last sentence which is the point in issue before the Court.

The draft letter went on to refer to the obligation of the mortgagee to install an evaporative air cooling system in the St James Theatre. There were then some provisions not presently relevant which were followed by a clause in the following terms:

> *"Lease - The parties will enter into a lease within two weeks of the date of this letter on the terms set out in the Auckland District Law Society Second Edition 1989 Deed of Lease amended in accordance with this letter and with such additional provisions as may be required by the landlord in relation to obligations under the Building Act and the Resource Management Act."*

On 22 January, which was, of course, the date on which the deal with Pacer Kerridge Cinemas was finally signed, and apparently in somewhat of a hurry because of a deadline relating to that matter, Mr Everard had further discussions with Mr Rofe about the draft letter. Mr Rofe had had to refer the draft to Mr Coney of SBSA. Mr Coney had jibbed at the rental of $200,000 for the 12 month period. Previously Pacer Kerridge Cinemas Ltd had been paying a so called occupancy fee at a level of $400,000 per annum. Whilst all concerned appreciated that the complex had been adversely affected by the multiplex opening at Wairau Park and by reason of the deterioration in its condition and also appreciated that even to

operate the complex satisfactorily on a short term basis Everard would need to make significant expenditure on repairs and maintenance, Mr Coney was anxious to extract as much return as possible. He therefore insisted on a rent of $250,000 for a 12 month period. Mr Everard agreed to this and so the figure in the letter eventually signed by Mr Rofe for rental was $250,000. The provisions quoted above relating to the term and the entry into a formal lease were unchanged. One of the conditions, relating to approval by SBSA's head office, was removed. The remaining condition, which was satisfied on the same day, was for entry into an unconditional agreement for Everard to purchase the business of Pacer Kerridge Cinemas Ltd and Nibble Nook Ltd.

No formal lease was ever concluded. I heard evidence about the preparation and submission to Everard's solicitors of a draft deed of lease and about certain negotiations which took place in relation to its terms. I will refer to that matter later in this judgment.

Later in 1993 while Everard was operating the movie theatres in the complex it made endeavours to obtain a right of first refusal and there were also discussions about the possibility of a longer term lease being granted. But by October 1993 SBSA had decided to offer the St James complex for sale by tender. The tender documents stated that the area of the complex with which this case is concerned was subject only to a one year lease from 1 February 1993. (That is clearly wrong, for the one year ran from 22 January, but nothing turns on this point.) They also stated that there was no right of renewal.

On 1 December Everard submitted a tender recording that it did so "under protest and without prejudice", saying that the tender was "out of

order" in holding out to tenderers vacant possession of the premises at the expiration of the current lease. The letter, which was written by Everard's solicitors, called for SBSA to negotiate in good faith the terms of a renewal of the lease. On 21 December the solicitors wrote again notifying SBSA of Everard's intention to renew its lease and called upon SBSA as mortgagee "to enter into negotiations accordingly".

The purported exercise of renewal was ignored by SBSA which, just before Christmas last year, entered into an agreement to sell the fee simple estate in the St James complex to the Village Force joint venture, which is a trade competitor of Everard. The price was $7,500,000. Settlement is due to take place on 28 May 1994. Upon settlement the purchaser is entitled to vacant possession. However, under clause 17 of the agreement it is conditional on the vendor obtaining vacant possession no later than three working days prior to the possession date. If this cannot be done the purchaser is entitled to cancel the agreement or, at its option, to require the vendor to take reasonable steps for a further period six months to obtain vacant possession, in which case the possession date is extended to 28 November 1994.

In the proceedings brought by Everard it seeks an injunction prohibiting re-entry by SBSA and a declaration that it is entitled to a renewal of its lease for a period of 12 months commencing 22 January 1994. It also seeks a declaration that it is the owner of the chattels and tenants' fixtures and fittings in and about the premises. In the agreement with Pacer Kerridge Cinemas the assets appearing to pass to Everard include the plant, fixtures and fittings situated in premises previously occupied by the vendor. These are said to include chattels and tenants' fixtures and fittings in the St James complex. Additionally, Everard says that it has brought certain items

(particular mention was made of some projectors) into the premises and that they remain its property. In the proceedings brought by SBSA it seeks an injunction restraining Everard from removing items from the theatre centre.

Pursuant to orders of Robertson, J. and Thorp, J. Everard remains in possession of the centre until further order of the Court. The two sets of proceedings have been consolidated. The question of ownership of items in the premises has been referred for determination by a referee. A preservation order has been made in respect of them pending that determination so that Everard is prohibited from removing them in the meantime. I should record that SBSA has advised, through Mr Davison, that if Everard is successful in establishing ownership of any chattels or that as tenant it has otherwise enjoyed a right of removal of any fixtures and fittings, SBSA will not assert that any such right has been lost because the items may not have been removed during the term of the lease. That, of course, presupposes that the Court finds that the lease has already come to an end.

An order has been made pursuant to r.418 for determination as a separate issue of the question of whether Everard is entitled to a renewal of the lease for a period of 12 months from 22 January 1994 and it is that issue which has been argued and is now the subject of this judgment. What did the parties mean by the following statement in the letter of 22 January 1993?:

> *"Prior to one month before the expiration of the initial term you would notify the Mortgagee in writing of your intention to enter into a further period of lease on terms acceptable to both yourselves and the Mortgagee."*?

This provision must, of course, be read in its context in the document and having regard to the background facts.

I refer for guidance to the well known passage of the judgement of Lord Wilberforce in ***Prenn v Simmonds*** [1971] 1 WLR 1381 at pp.1383-4:

> *"In order for the agreement ... to be understood, it must be placed in its context. The time has long passed when agreements, even those under seal, were isolated from the matrix of facts in which they were set and interpreted purely on internal linguistic considerations. ... We must ... 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 Lord Wilberforce rejected any idea that it was permissible to have regard to the course of negotiations between the parties leading up to the making of the agreement. He pointed out that in the nature of things the positions of the parties changed during negotiations and are until final agreement, though converging, still divergent. "It is only the final document which records a consensus." Previous documents may be looked at only for the limited purpose of deducing the commercial or business object of the transaction, objectively ascertained. That is a surrounding fact. Having made this point, Lord Wilberforce p.1385 went on:

> *"And if it can be shown that one interpretation completely frustrates that object, to the extent of rendering the contract futile, that may be a strong argument for an alternative interpretation, if that can reasonably be found. But beyond that it may be difficult to go: It may be a matter of degree, or of judgment, how far one interpretation, or another, gives effect to a common intention: the parties, indeed, may be pursuing that intention with differing emphasis, and hoping to achieve it to an extent which may differ, and in different ways. The words used may, and often do, represent a formula which means different things to each side, yet may be*

> *accepted because that is the only way to get "agreement" and in the hope that disputes will not arise. The only course then can be to try to ascertain the "natural" meaning. Far more, and indeed totally, dangerous is it to admit evidence of one party's objective - even if this is known to the other party. However strongly pursued this may be, the other party may only be willing to give it partial recognition, and in a world of give and take, men often have to be satisfied with less than they want. So, again, it would be a matter of speculation how far the common intention was that the particular objective should be realised."*

Returning to the subject in ***Reardon Smith Line Ltd v Hansen-Tangen*** [1976] 3 All ER 570 at p.574 Lord Wilberforce said:

> *"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 had in mind in the situation of the parties."*

I have already set out in this judgment what I regard as being the salient factual background. I add reference to one other matter, which is a note made by Mr Rofe contemporaneously of his conversation with Mr Everard on 7 January, but I emphasise that I look at this document only to see whether it casts light, objectively, on the commercial or business object of the ultimate transaction. He records a position said to have been put to him by Mr Everard. He sets out some suggested terms "in the event of St James becoming available to lease and operate". He refers, firstly, to a period of six months and six months "with right to formalise a long term agreement based on the draft heads of agreement which were earlier discussed". This seems to be a reference back to a draft submitted in August 1992. After reference to rental and rates, the note makes mention

that SBSA will not contribute anything for upgrade of the cinemas during the period. Then it is recorded that:

> *"Assessment can then take place of the redevelopment programme for the theatre complex."*

Before I proceed to set out my interpretation of the crucial provision I must briefly say something about the status of the evidence which was given before me, and the documentation, relating to dealings between the parties after 22 January 1993. In particular, there was the draft deed of lease and correspondence and notes of discussions about negotiations for changes to the draft document. SBSA sought to use these materials to prove that Everard did not at that time believe that it had any right to a renewal of the one year term. However, when I questioned whether the Court was entitled to construe the agreement to lease by reference to the positions subsequently taken, or apparently taken, by the parties, Mr Davison conceded that this was not appropriate except perhaps where there was an issue of credibility. He referred me to ***McLaren v Waikato Regional Council*** [1993] 1 NZLR 710 at 731.

In England it seems to be established by ***Schuler AG v Wickman Machine Tool Sales Ltd*** [1974] AC 235 that evidence of the parties' post-contractual behaviour is not admissible to show their intentions. The point remains open in New Zealand, having been left so by the Court of Appeal on several occasions. On the most recent of these, Cooke, P. in his judgment in ***Offshore Mining Co. Ltd v Attorney-General*** (unreported, 28 April 1988, CA 116/86) commented that it was:

> *"...quite rarely that the post-contract conduct of both parties can be labelled unequivocal for the purpose of interpreting their contract."*

If this means that where both parties plainly adopt the same interpretation, evidence can be received of that fact for purpose of interpretation of the contract (as opposed to an argument based on estoppel by convention), nevertheless I would not find it helpful to do so in the present case. Had I taken into account the dealings of the parties concerning the draft deed of lease they would certainly have pointed in the direction of confirming the view which I will shortly express as to the meaning of the provision in question, but I am not in a position to say that their conduct can be labelled completely unequivocal and I therefore think it best to disregard this material.

I begin from the position that the final sentence of clause 2 of the letter of 22 January 1993 is not, when read by itself, noticeably ambiguous. It refers to the expiration of the initial term of 12 months and appears to say that Everard "would notify" SBSA in writing of its intention to enter into "a further period of lease on terms acceptable to both" Everard and SBSA. Notification is clearly optional but also a pre-condition. It seems to me, however, that the critical factor is the reference to the acceptability to both parties of the terms which are to relate to the "further period".

If the sentence had ended with the words "further period of lease" it could well have been read as conferring a right of renewal for a period of 12 months. A bare reference in a lease to a right of "renewal" or to a right to "re-lease" without mention of the period of time involved have each been read as giving the lessee the right to repeat the original term: ***Lewis v Stephenson*** (1898) 67 LJ QB 296; *Malfroy v Raymond* (1907) 26 NZLR 563. And in *Austin v Newham* [1906] 2 KB 167 where a tenant entered into possession of premises under an agreement of tenancy "for a period of

12 months with the option of a lease after the aforesaid time" it was held that the tenant had a right to a lease for a further period of "at least one year" after the expiry of the initial term.

However, these cases are distinguishable because, even if it is accepted that when speaking of "a further period" Mr Rofe meant a further period of 12 months (which taking into account the background circumstances is unlikely), the whole position is qualified by the need for acceptability to both parties of the terms to apply to the period of renewal. Mr Ingram argued that it must have been the common intention that any disagreement about the acceptability of terms should be settled by arbitration. The arbitration clause to which he referred is that contained in the Auckland District Law Society's Deed of Lease form. This is the form of lease mentioned in paragraph 7 of Mr Rofe's letter. However, I doubt that one could describe terms settled, and therefore imposed, by an arbitrator as being terms necessarily "acceptable" to a party having them imposed upon it. "Acceptable" is, of course, the language of offer and acceptance, of a concluded negotiation rather than of an arbitral award.

Further, though it is I think unnecessary to place much weight on the point, it may be doubtful that the arbitration provision in the lease form is to apply until the formal deed of lease has been negotiated and entered into. One cannot overlook the need for settlement in some manner of the additional provisions to be required by the landlord relating to the Building Act and the Resource Management Act. It seems to me that the arbitration clause may not be intended to operate until the lease itself has been concluded.

To this point I have looked at the provision relating to the "further period" just as it stands in the letter of 22 January 1993 but the position does not, in my view, change at all when one has regard to the factual background. It was common ground that there was to be an initial period of one year so that Everard could have the opportunity of running the theatre complex, see how it performed and investigate the possibility of a more substantial involvement. Significant expenditure would be required in the short term. That seems to have been reflected in the level of rental fixed for the 12 month period. That period was also long enough to enable some recoupment of the expenditure from receipts of trading. But, looking at the matter objectively, the parties also had to recognise the need for SBSA as mortgagee to recover its money by selling the centre as soon as possible. The rental was not adequate to service the loan. A long term lease (say seven years, which was the maximum that the mortgagee could grant) would provide an income stream for an investor over the medium term future. A further period of lease of one year only would be quite unsatisfactory for this purpose. Nor, it seems to me, would an additional period of one year only much advance the position of someone like Everard, seeking security of tenure.

Looking at the background to the letter of 22 January and restricting myself as is required by the authorities to which I have referred, I have little difficulty in coming to the conclusion that when the parties referred to a "further period" they were addressing a long or medium term (up to seven year) lease and were simply recording an intention that at the end of the 12 month period, if Everard wished, there might be an attempt to negotiate such a lease. There is no intention to be bound to a further term. In this respect the case has some resemblance to ***Aitken v Regent Theatre Co. Ltd*** (1934) GLR 331. The requirement for the giving of a notice one month

before expiry of the initial term is explicable by Mr Rofe's need to have a period of at least a month in which to make arrangements for someone else to take over the operation of the cinemas (or to get ready to do it himself) if Everard did not want to pursue the matter. In the absence of a notice from Everard by 22 December 1993 Mr Rofe would know that he had to proceed accordingly.

For the foregoing reasons I find that Everard was not entitled to renew its lease after the initial term of 12 months. Both counsel agreed that if I took this view there should be an order of the Court for the yielding up of possession of the premises which ought to give Everard a period of about seven days from the date of the delivery of the judgment within which to wind down its operations. In particular there is a need for termination of employment contracts connected with the complex and contracts for the advertising of movies currently being screened. There will, therefore, be an order that Everard shall vacate and deliver up the premises to SBSA no later than 4 p.m. on 25 May 1994.

I also heard argument as to the terms upon which the preservation order in respect of the chattels, fixtures and fittings should now be continued pending the referee's determination. Everard's concern is that if SBSA proceeds to settle the sale of the St James complex to Village Force and possession passes upon settlement, then Village Force, one of its competitors, will make use of items which may ultimately prove to have been all along the property of Everard or which Everard may all along have been entitled to remove (thus gaining title to the former fixtures). I made the suggestion that one of the terms of the preservation order might be a requirement for payment of rental by any user based on the market value of the items in question. However, the position taken by Everard has been

that it will not consent to any such term and that the Court has no power to sanction by this means a trespass or conversion by Village Force. Whether or not I regard the attitude taken by Everard as sensible (damages for any trespass or conversion may be fixed at a level below an assessed market rental), I think the point is well taken and I do not propose to make an order which expressly sanctions anything that may be done by Village Force. On the other hand, the Court will not, unless the matter is further brought before it, make an order which inhibits the giving and taking of possession pursuant to the existing agreement for sale and purchase with the items in question in situ.

There will be an order continuing the preservation order made by Thorp, J. on 19 April (as varied on 20 April), which is now further varied as follows:

(a) As from the time when Everard vacates possession of the St James Centre Complex the items covered by the preservation order are to be at the risk of SBSA (whether or not the premises are from time to time thereafter in the possession or occupation of any other party) to the intent that SBSA is to be responsible to Everard for any loss of or injury to such of those items as the referee may determine Everard to be entitled to.

(b) SBSA is not to use or permit any other party to use any projector first brought into the premises by Everard and such projectors are prior to transfer of possession by SBSA to be placed in storage in the storage area within the premises.

(c) SBSA is to be responsible for ensuring that if the referee determines that any item is one to which Everard is entitled, Everard is immediately able to remove the item from the premises, having a reasonable period within which to do so, free of any claims by SBSA or any person claiming through SBSA (including Village Force).

(d) The expense involved in removing any item which the referee finds Everard to be entitled to, together with the expense of reinstating any damage caused thereby, is to be borne by Everard.

Costs are reserved.