IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV 2008-404-006936

	BETWEEN	LPS MANAGEMENT LIMITED Plaintiff
	AND	FUN WORLD CENTRE (FIJI) LIMITED Defendant

Hearing: 7 July 2009

Counsel: A V Ram for plaintiff
M C Black for defendant

Judgment: 23 December 2009 at 5:00pm

JUDGMENT OF ASSOCIATE JUDGE ABBOTT

This judgment was delivered by me on 23 December 2009 at 5:00pm, pursuant to Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Solicitors:
A Kashyap, PO Box 29596 Auckland 1344 for plaintiff
D M Bahadur, PO Box 1984, Auckland 1140 for defendant

[1] This case involves a dispute over a contract for supply of equipment for an aquatic park in Fiji. The defendant, Fun World Centre (Fiji) Limited (FWC), is the developer of the park. It entered into a contract with the plaintiff, LPS Management Limited (LPS), for the supply and installation of water slides and other equipment for the park to a total value of $2,475,000.

[2] FWC has purported to cancel the contract. LPS is suing FWC for damages of $400,000 for breach of specific terms of the contract, or alternatively for $372,261 for losses suffered due to wrongful repudiation. FWC denies any breach and counterclaims alleging breach and misrepresentation by LPS. In effect it is seeking return of a deposit of $500,000.

[3] FWC has applied for an order the LPS give security for its costs in the sum of $94,000. LPS opposes the application on the grounds that FWC has not shown that it will be unable to pay costs if its claim is unsuccessful, and that the Court should in any event exercise its discretion in LPS' favour. It says that FWC's application is no more than a strategem intended to prevent it from pursuing its claim.

[4] For the reasons I shall now give I have come to the view that the application cannot succeed at this time.

Factual background

[5] As applications for security for costs are determined on a case by case basis, it is appropriate to set out background facts briefly before considering the principles that the Court has to apply and addressing the opposing arguments.

[6] LPS was incorporated on 3 August 2004. It has its registered office in Auckland but operates from premises in Hamilton. It says that it carries on business in New Zealand and around the world as a supplier, installation supervisor, and commissioner of aquatic park equipment. FWC is registered in Fiji but has a place of business in Auckland.

[7] In 2006 parties associated with FWC embarked on a substantial commercial development to be known as the Fun World Centre on land near Nadi. Although there is no evidence on the point, it appears that FWC is the vehicle for carrying out the development. The development was to have included a hotel, retail shopping outlets and an aquatic park.

[8] A company associated with one of the directors of FWC, Shah Homes Limited, engaged an architectural company, Hames Sharley International (NZ) Limited, in early to mid 2006 to undertake design work and manage the project for a consultancy fee of $1,250,000. The terms of the engagement were recorded in a formal agreement (the consultant agreement). Hames Sharley embarked on design work, which included overall layout of the site. A layout plan, including the aquatic park, had been prepared by March 2007.

[9] On or about 2 May 2007 FWC entered into a formal agreement with LPS for LPS to supply equipment for the aquatic park, and to supervise its installation and undertake its commissioning (the agreement). The work was identified by reference to the overall design for the aquatic park that had been prepared by Hames Sharley. The total contract price was $2,475,000. The agreement included provision for payment of a deposit at the time that FWC placed the order, and staged payments thereafter. It also required FWC to provide LPS with an irrevocable letter of credit prior to the start of the manufacture of any equipment to secure the contract payments and allow for progressive deliveries. The agreement set out a time frame for the work, leading to an anticipated opening date of 1 December 2007. The agreement stipulates that LPS was to report to the Project Manager Architect (Hames Shanley).

[10] FWC paid LPS the deposit of $500,000 upon execution of the agreement. Although this is not accepted by FWC, LPS says that the deposit was used in the purchase of equipment for the project, particularly wave-making equipment and a water treatment plant. It says that the requisite items were ordered in June 2007.

[11] LPS also says that detailed designs for wave-making equipment, suitable pool shapes and size, and for a machinery room were provided and signed off, and filter

plant components were pre-ordered. Again, FWC challenges LPS about this, saying that it has been given no documentation to support what LPS claims. Apart from a letter by LPS' director Mr Dawson, there is no evidence before the Court of any orders placed or payments made in respect of them, nor of any design work undertaken by LPS.

[12] On 6 June 2007 LPS issued an invoice for the second instalment under the agreement ($400,000). It is common ground that this invoice has not been paid. It also appears that LPS requested the establishment of a letter of credit at that time, to cover the balance of the contract payments (three payments totalling $1,575,000).

[13] It appears that there were a number of meetings between LPS and Hames Sharley (and perhaps other FWC representatives but there is no specific evidence on this before the Court) between June and September 2007. There is no evidence as to whether or not LPS' second invoice was discussed at these meetings, although there is reference in correspondence to unmet promises of payment made by FWC's director Mr Shah.

[14] The project, including the contract between LPS and FWC, had a major setback when Hames Sharley went into liquidation on 15 October 2007. There is a paucity of evidence as to what occurred at that point, but it appears that FWC decided to manage the project itself. Certainly, it did not appoint another project manager.

[15] There is no evidence before the Court as to the status of the project as a whole, or the agreement between FWC and LPS in particular, at the point that Hames Sharley went into liquidation or until late February 2008. What is apparent is that the project had fallen way behind schedule, and by early 2008 the completion date had been pushed out to November 2008.

[16] By the end of February 2008 the relationship between FWC and LPS was deteriorating. LPS was calling for payment of its invoice for the second instalment under the contract, and FWC was seeking information as to progress under the contract. A project review meeting was held in early March 2008. There are no

minutes of the meeting before the Court, but in a letter written the following day LPS' director Mr Dawson refers to FWC resisting payment of the second invoice until it was given information about LPS' uses of the deposit. Mr Dawson took the position that LPS was not contractually obliged to justify the application of that deposit but provided information "so that it gives you some comfort where the funds are been applied".

[17] Mr Dawson also wrote the same day again requesting a letter of credit to cover the balance of the contract instalments.

[18] By the end of March 2008 (and it seems for some time before this, although again the evidence is not before the Court) FWC was challenging LPS over the scope of the contract, as well as its use of the deposit. It was taking the position that a new contract was needed to address its concerns, and was threatening to abandon the existing agreement. There was an issue, in particular, over one aspect of the aquatic park (the size of a wave pool) and responsibility for its design.

[19] On 15 April 2008 the solicitor for FWC wrote to the solicitor for LPS giving notice that FWC terminated the agreement. The grounds given for termination were LPS' failure to provide appropriate information as to the work that it had completed, an alleged failure to comply with deadlines, and an alleged failure to carry out the work to a reasonable professional standard. FWC sought return of its deposit.

[20] LPS responded saying that it was ready to perform its obligation under the agreement. However, after exchanges of correspondence between respective lawyers, LPS accepted FWC's repudiation and cancelled the agreement.

[21] LPS issued this proceeding on 17 October 2008. FWC filed a defence and counterclaim on 9 December 2008. Following receipt of the proceedings, FWC's counsel wrote to LPS' solicitors (on 19 November 2008) requesting evidence of its ability to pay costs. In a follow-up letter (written on 4 December 2008) counsel for FWC refers to advice that LPS' accounts show shareholders' funds of approximately $44,000, but expresses the view that that did not satisfactorily answer FWC's concerns. The present application was filed on 5 February 2009.

Cross application

[22] In its notice of opposition and the affidavits in support of the opposition LPS asks the Court to order FWC to put up security and its directors (Messrs Khan and Shah) to be liable for LPS' costs in the proceeding. It contends that FWC does not have an ongoing business operation or any cash flow and that the directors personally are funding the litigation. In the alternative, LPS seeks an order that the directors be made party to the proceeding so that the orders for costs can be made against them.

[23] These are matters which should be brought properly before the Court in a formal application. It is not appropriate merely to "tack them on" to a notice of opposition to FWC's application for security. In particular any application for orders affecting the directors need to be served on them personally. LPS may well have grounds for these applications, but they need to be addressed in the ordinary course. Counsel will also need to give greater consideration to the supporting evidence. He has been critical of the lack of evidence in support of FWC's application. Even if I had been prepared to allow LPS to bring an application informally in this manner, I would expect substantially more cogent evidence to support it.

Principles to be applied

[24] The application is made under r 5.45 of the High Court Rules. The applicable parts of that rule, for the purpose of the present application is:

> **5.45 Order for security of costs**
>
> (1) Subclause (2) applies if a Judge is satisfied, on the application of a defendant,—
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> ….
>
> (b) that there is reason to believe that a plaintiff will be unable to pay the costs of the defendant if the plaintiff is unsuccessful in the plaintiff's proceeding.
>
> (2) A Judge may, if the Judge thinks it is just in all the circumstances, order the giving of security for costs.
>
> (3) An order under subclause (2)—

(a) requires the plaintiff or plaintiffs against whom the order is made to give security for costs as directed for a sum that the Judge considers sufficient—

(i) by paying that sum into court; or

(ii) by giving, to the satisfaction of the Judge or the Registrar, security for that sum; and

(b) may stay the proceeding until the sum is paid or the security given.

….

(6) References in this rule to a plaintiff and defendant are references to the person (however described on the record) who, because of a document filed in the proceeding (for example, a counterclaim), is in the position of plaintiff or defendant.

[25] The general approach that the Court takes to such applications can be found in the decision of the Court of Appeal in *A S McLachlan Limited v A M Network Limited* (2002) 16 PRNZ 747 at para [13]-[16]. For the purpose of the present application the following are the relevant principles:

a) The applicant must meet a threshold test, namely show that there is reason to believe the plaintiff (and in this case also the defendant) will be unable to pay costs if unsuccessful.

b) Once the threshold test has been satisfied, the Court has a discretion, to be exercised in all the circumstances of the case, whether or not to order security and, if so, as to the amount to order.

c) The discretion is to be exercised after a careful assessment of the circumstances of the particular case.

d) The rights of both parties are to be weighed in the exercise of the discretion. On the one hand, an order which will have the effect of preventing a plaintiff pursuing a claim should be made with caution, and only if the claim has little chance of success. On the other hand, defendants must be protected against being drawn into unjustified

litigation, particularly in respect of claims which are overly complicated and necessarily protracted.

The competing arguments

(a) The threshold requirement – ability to pay

[26] FWC relies on three matters to support its contention that there is reason to believe LPS will not be able to pay its costs if the claim does not succeed. It refers to the limited information available as to its financial position: the fact that LPS has only 100 shares (all held by its director, Mr Dawson) and advice from LPS' solicitor that it has shareholders' equity of only $44,000. It says that the Court can take into account LPS' failure to provide information about the use to which the deposit of $500,000 has been put. Thirdly it relies on a statement made by a representative of Hames Sharley (at a meeting on 31 March 2008) that LPS was known to be facing several demands, and that that information had not been rebutted. Counsel submitted that in those circumstances the Court was able to, and should, draw an adverse inference from LPS' failure to respond to requests for information as to its financial position: *NZ Kiwifruit Marketing Board v Maheataka Coolpack Limited* (1993) 7 PRNZ 209, 212-3.

[27] Counsel for LPS submitted that FWC had failed to provide any, let alone sufficient, evidence that LPS was unable to pay. He submitted in addition, that although the onus lay on FWC and LPS had no obligation to provide financial information, it had given evidence that it was solvent (able to pay its debts as they fell due) and had a number of large contracts for engineering services in New Zealand and with overseas governmental organisations. He referred to LPS' evidence that it had reported steps taken to the project manager (Hames Sharley) as it was required to do and, although contending that there was no further obligation he referred to Mr Dawson's advice to FWC in March 2008 as to how the deposit had been applied. He submitted that the only possible evidence of inability to pay was the comment made to FWC by Hames Sharley's representative in the meeting on 31 March 2008, but said that that was hearsay and could not stand against the evidence

of LPS' accountant (whose offices were LPS' registered office) that she was not aware of any demands having been made on LPS.

(b) Discretion

[28] The principal factor raised by counsel in relation to the Court's discretion were their respective perceptions of the merits of the case.

[29] Counsel for FWC submitted that the merits were significantly in favour of his client. He said that FWC's view of LPS' breaches had been clearly put both in correspondence, in its counterclaim and in the affidavit of its solicitor in support of the application for security. He contended that the arguments had not been satisfactorily answered by LPS in the correspondence, and LPS had failed to comply with a direction to provide a more specific response to the assertions in the counterclaim. He also argued that LPS was clearly in breach of a requirement to provide evidence of its performance of its obligations under the contract, and had clearly misrepresented its relevant contract experience on such development. Finally he argued that LPS' demand for a letter of credit was not in accordance with the contract and LPS, in any event, had waived that contractual requirement.

[30] Counsel for LPS argued to the contrary that the merits were strongly in favour of his client. He submitted that his client had met its contractual obligations, and FWC was clearly the party in breach, having failed to pay the second contract instalment some months before the other issues were raised by FWC. He argued that LPS had reported, as required, to the project manager in meetings held between June and September 2007 (referring to minutes of those meetings) and relied on the terms of the consultant agreement and the agreement between FWC and LPS in support of a submission that design responsibility for the wave pool (one of the major areas of contention) clearly lay with Hames Sharley not with LPS. He argued that FWC had failed to provide all the information needed to allow LPS to complete its side of the contract, and said that the contract was clear that the letter of credit had to be in place before start of manufacturing, and the issues over its terms had not been raised until shortly before FWC purported to terminate the contract.

Discussion

[31] I accept the submission of counsel for LPS that FWC has not established that LPS will be unable to pay costs if its claim fails. The limited financial information available is in favour of LPS. The number of shares issued in LPS give no information as to its financial means. Secondly, the shareholders' equity of $44,000, although reasonably modest (having regard to the size of the contract) seems supportive of an ability rather than an inability to pay.

[32] Counsel for FWC suggested in oral argument that LPS' alleged failure to complete design work and to produce evidence of expenditure of the deposit indicated financial difficulty. However, those allegations are strongly disputed, and there is no evidence of complaints of this nature in the period when the project was being managed by Hames Sharley (one would expect them to be mentioned in minutes of project meetings).

[33] The only possible evidence of financial difficulty, in my view, is to be found in the evidence of the solicitor for FWC that a representative of Hames Sharley indicated in a meeting with him on 31 March 2008 that "LPS is likely to be insolvent and has a few statutory demands against it". This is clearly hearsay although it is potentially admissible if it complies with r 9.76(1)(d)(i) of the High Court Rules (by reason of s 20 (1) (of the Evidence Act 2006). It does not comply. To do so it has to satisfy the test of general admissibility of hearsay (for trial) in s 18 of the Evidence Act 2006. However, there is no evidence that the Hames Sharley representative (a Mr Tony Ram) is unavailable, or that undue expense or delay would have been caused if he was required to give an affidavit in this application. More significantly, it is directly in conflict with the evidence of LPS's accountant (Ms A Chen) who has given evidence as follows:

> "I have not received any demands against the plaintiff. We are the registered offices of the plaintiff and would be the first to receive any demands should there be any."

[34] The rest of the "evidence" on which FWC relies is LPS' failure to respond to FWC's continuing requests for detailed information about the application of the deposit money, and subsequently its failure to respond to FWC's requests for

evidence of its ability to pay costs. As to the former, FWC has not rebutted LPS' evidence that it provided this information to the project manager in the period June to September 2007. It was open to FWC to call evidence from Hames Sharley to challenge this, possibly by reference to project minutes. There is nothing to suggest that Hames Sharley had any concerns. The evidence before the Court is that FWC's concerns were not voiced until late February 2008. However, there is also evidence before the Court, in an affidavit by a contractor on the site, the FWC itself is in financial difficulty. Although the timing is not clear, LPS' director Mr Dawson refers in his letter of 7 March 2008 to FWC's "recent negative experiences with your builder in Fiji and Hames Sharley". This all suggests a substantial measure of self preservation in FWC's allegations rather than any real basis for concern about LPS' solvency.

[35] I do not consider that this is a case where an adverse inference can or should be drawn from the fact that LPS did not respond to a request to provide financial information about itself. The following passages from *NZ Kiwifruit Marketing Board v Mahetatake Coolpack Limited* are apposite (at 212 and 213):

> The question is always whether it is appropriate to draw an adverse inference against the plaintiff because of his or her silence as to their financial position. Whether it is appropriate is a question which can only be determined having regard to the material before the Court in each case.
>
> ....
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> There must be some evidential foundation or indication to support the charge that there is reason to believe that the plaintiff will be unable to pay the costs before the Court is justified in drawing an adverse inference from the absence of a positive response from the plaintiff. In my view, the Court should look for some basis in the circumstances which would give rise to an expectation that the plaintiff should proffer information to counter the suggestion that he or she is not able to meet a cost award.

In light of the matters that I have mentioned above I find that there is an insufficient evidential foundation to justify drawing an adverse inference.

[36] Given that FWC has not established that LPS is unable to meet potential cost orders, it is not necessary for me to consider whether or not I should exercise my discretion to award security. Nevertheless, as counsel addressed this in argument, I will deal with those arguments briefly.

[37] I have already made the point that the only factor advanced by counsel for FWC was that the merits were strongly in his client's favour. The first point that needs to be made in that respect is that there is a limit as to how far the Court can make a judgment on the merits at an early stage of the proceeding: *Meates v Taylor* (1992) 5 PRNZ 524 (CA).

[38] I turn now to the various matters advanced in respect of the merits. Although it is not possible to make an informed assessment of the merits on the evidence before the Court, the following factors in my view suggest that the merits are relatively evenly balanced, but favour LPS:

a) At the outset the agreement had a comparatively short completion time (some seven months). It is entirely consistent with that timeline that LPS would have used the deposit to order equipment promptly after signing the agreement as it contends. It is equally consistent that it would have invoiced the second instalment within a month or so of commencement, and would have sought a letter of credit at that time.

b) FWC has put forward no evidence to refute LPS' statements that they embarked on the procurement of equipment for the project (including the substantial component of the wave-making equipment and water treatment plant for the wave pool) upon signing of the agreement and payment of the deposit, and using the deposit for that purpose. One would expect FWC to have produced evidence from someone at Hames Sharley if Hames Sharley had a different view (and to have produced some documentary evidence of this from project minutes).

c) Hames Sharley appears to have had overall design responsibility for the project. It is difficult to see exactly what design responsibility LPS may have had for the wave pool which is clearly a source of major dissention.

d) There is nothing to suggest that there was any concern about LPS' performance whilst Hames Sharley was acting as project manager.

e) There is no evidence suggesting that lack of performance was the reason initially for not paying the second contract instalment in 2007 (LPS' solicitors remark on this in their letter of 30 May 2008).

f) There were clearly difficulties with the project unrelated to the agreement between FWC and LPS. Although it is likely that this caused FWC to review its position under the agreement(and its wish to renegotiate that it) , that is quite a different matter from an allegation of breach by LPS. Indeed, it appears that the completion date for the project had already been put back to November 2008 by the time that FWC and LPS started discussions in earnest on their agreement.

g) The terms of the agreement are clear that a letter of credit was to be in place before start of any manufacturing, so as to allow for progressive deliveries. Even if LPS requested a letter of credit in different terms, that did not stop FWC tendering one on the correct contractual basis. More significantly, it did not stop FWC from either paying the second instalment on a timely basis or (if this was the case) putting forward its case for breach immediately after receiving that invoice (sometime in June 2007).

h) Although it seems arguable, in principle, that FWC should be entitled to receive information from LPS about its performance of the contract, it also appears to be arguable that LPS did comply with this obligation (by provision of information to Hames Sharley) and that FWC ought to have been able to obtain that information from Hames Sharley. Having said that, there does not seem to be any good reason why LPS could not have given FWC the information.

i) There are some unanswered questions about the clause in the agreement setting out LPS' work history/experience. However, that point is not entirely clear. It appears that the agreement was drafted by FWC's lawyers, and there could have been some misunderstanding

> as to what LPS was saying about the reference to other sites. It is possible that it was merely saying that they were sites where there was a theme linking hotels and shopping centres to aquatic environments (as was being proposed in this development) rather than saying that it had an active or substantial role in those other developments.

[39] I am not prepared to draw an adverse inference on the merits from LPS' failure to file a detailed response to FWC's pleading of its counterclaim by the time of the hearing. Counsel for LPS advised in the hearing that this was due to difficulty obtaining evidence in time. I note that a detailed reply was filed two days after the hearing.

[40] Counsel for LPS raised two other related points which he submitted should cause the Court to refine an order in any event. He argued that the application was merely tactical. He also referred to the comments of the Court of Appeal in *A S McLachlan Limited v MEL Network Limited* (at para [15]) that an order for substantial security could prevent a plaintiff from pursuing its claim, and should only be made after careful consideration and in a case in which the claim has little chance of success.

[41] Although there are unanswered questions about the effect of other problems on the site upon this contract, I am not prepared to find on the strength of the evidence before the Court that the application is purely tactical. The evidence advanced for LPS is too general and vague to persuade me to draw that conclusion.

[42] Counsel's second point is potentially inconsistent with his earlier argument that there was no reason to believe that LPS was unable to meet costs. Nevertheless, I do not regard that as sufficient to cause me to revisit my earlier finding that FWC has not established an inability to pay. Nevertheless it raises the possibility that further information could become available to warrant a reconsideration of the application. That remains open to FWC.

[43] Weighing these various matters I am not persuaded on the evidence before the Court that it would be in the interests of justice in this case to order LPS to provide security at this time.

Decision

[44] FWC has not established that LPS will be unable to pay costs in the event that its claim fails. The application is dismissed.

[45] As the successful party, LPS is entitled to costs on a 2B basis.

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Associate Judge Abbott