IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2008-404-8214

	IN THE MATTER OF	Section 143 of the Land Transfer Act 1952
	BETWEEN	CAPITAL + MERCHANT INVESTMENTS LIMITED (IN RECEIVERSHIP) AND CAPITAL + MERCHANT FINANCE LIMITED (IN RECEIVERSHIP) Applicants
	AND	RUSSELL MANAGEMENT LIMITED Respondent

Hearing: 19 and 22 December 2008

Appearances: S Barker for Applicants
PV Shackleton for Respondent

Judgment: 22 December 2008

JUDGMENT OF ASHER J

Solicitors:
S Barker, Buddle Findlay, PO Box 2694, Wellington
PV Shackleton, Martelli McKegg Wells & Cormack, PO Box 5745, Wellesley Street, Auckland

Introduction

[1] This is an urgent application by Capital + Merchant Investments Limited (In Receivership) and Capital + Merchant Finance Limited (In Receivership) ("Capital"), at the behest of the receivers for those companies for the removal of a caveat. The caveat is registered against a property over which Capital has a mortgage. Russell Management Limited ("Russell Management"), has been a lessee of certain units on that property.

[2] The property has been sold, and was due to settle on 5 December 2008. As I will set out shortly, the caveat was registered only on 2 December 2008 (after the agreement for sale and purchase was entered into), and for reasons that will be set out in more detail, it is not the applicant's fault that there is this urgency. It is necessary to give an oral judgment, given the proximity of Christmas.

Background

[3] Capital is a mortgagee of seven units at a luxury resort in Russell known as 'Russell Cottages'. The owner of the properties is Winslow Group Limited ("Winslow"). Winslow had leased the seven units to Russell Management. The Capital mortgages with Winslow as mortgagor, were registered in January 2005.

[4] The sample lease provided on behalf of Russell Management shows a lease entered into on 1 February 2006 between Russell Management and Winslow for an initial term of ten years. None of the seven leases were registered, but they appear to be in registerable form. Under the leases, Russell Management was able to sub-lease the units for the purposes of the hotel on which it would receive a commission. The net revenue from the sub-leases of the units was payable to Winslow as lessor and owner of the units.

[5] On 17 January 2008, Capital issued and served notices against Winslow under s 119 of the Property Law Act 2007, on the basis that Winslow had gone into receivership. On 2 May 2008, Winslow was placed into liquidation. On

29 August 2008, under s 269(4) of the Companies Act 1993, the liquidators of Winslow disclaimed the seven leases.

[6] In September 2008, Russell Management wrote to the liquidators requesting a reconsideration of the decision. It was observed that these were good forward bookings. In the second letter, Russell Management said it was prepared to let the units from Winslow on the same terms as the disclaimed leases. The liquidators do not appear to have responded to the letters.

[7] On 5 November 2008, a locksmith changed the locks on four of the seven units. On 12 November 2008, Capital exercising its power of sale as mortgagee entered into an agreement to sell the seven units. The agreement was to be settled on 5 December 2008 and vacant possession was to be provided on that settlement.

[8] It appears that the then solicitors for Russell Management were aware of the existence of the sale contract from at least 19 November 2008. On 25 November 2008 the liquidator issued trespass notices to Russell Management. On 26 November 2998, the locksmith returned and completed the changing of the locks.

[9] On 2 December 2008, the caveat was lodged. The caveat sets out the claimed interest in the land as follows:

> An interest by virtue of lease instruments dated 1 February 2006 in respect of the land contained in the above certificates of title and made between the caveator as lessee and the registered proprietor as lessor.

[10] This application was made on 5 December 2008 and set down for hearing on Friday 19 December. It was called on that day at 4:15 pm and continued on Monday afternoon.

Approach to this application

[11] A caveator must establish an arguable case that it has an interest in the land: *Guardian Trust and Executors Company of New Zealand v Hall* [1938] NZLR 1020 at 1025. It is not enough to show that the lodging and continued existence of the

caveat is in some way advantageous to the caveator. An arguable case for claiming the interest must be shown. Delay is a relevant factor to be weighed in the exercise of the Court's wider discretion under the sections. Delay is more important where there is specific prejudice. What is required is a consideration of all the circumstances: *Varney v Anderson* [1988] 1 NZLR 478 at 480.

Section 269 of the Companies Act 1993

[12] Section 269 provides:

> **269 Power to disclaim onerous property**
>
> (1) Subject to section 270 of this Act, a liquidator may disclaim onerous property even though the liquidator has taken possession of it, tried to sell it, or otherwise exercised rights of ownership in relation to it.
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> (2) For the purposes of this section, onerous property—
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> (a) Means—
>
> (i) An unprofitable contract; or
>
> (ii) property of the company that is unsaleable, or not readily saleable, or that may give rise to a liability to pay money or perform an onerous act; or
>
> (iii) a litigation right that, in the opinion of the liquidator, has no reasonable prospect of success or cannot reasonably be funded from the assets of the company;
>
> …
>
> (3) A disclaimer under this section—
>
> (a) Brings to an end on and from the date of the disclaimer the rights, interests, and liabilities of the company in relation to the property disclaimed:
>
> (b) Does not, except so far as necessary to release the company from a liability, affect the rights or liabilities of any other person.
>
> …
>
> (5) A person suffering loss or damage as a result of a disclaimer under this section may—

(a) Claim as a creditor of the company for the amount of the loss or damage, taking account of the effect of an order made by the Court under paragraph (b) of this subsection:

(b) Apply to the Court for an order that the disclaimed property be delivered to or vested in that person.

(6) The Court may make an order under subsection (5)(b) of this section if it is satisfied that it is just that the property should be vested in the applicant.

[13] It is to be noted that under s 269(3) it is stated that the "disclaimer brings to an end on and from the date of the disclaimer the rights, interests and liabilities of the company in relation to the property disclaimed."

[14] Section 284(1)(b) states that on the application of various persons including "a creditor" a Court may confirm, reverse or modify an act or decision of the liquidator. Under s 269(5) a person suffering loss or damage as a result of a disclaimer under the section may claim as a creditor of the company, and therefore it would appear that a person claiming loss or damage arising out of a disclaimer can claim to be a creditor and apply under s 284.

[15] Mr Shackleton for Russell Management has proceeded on the basis that this is so. The issue that arises in relation to this application is whether the disclaimer of the lease that was made, brought the lease to an end and any rights of Russell Management as lessee and any interest in the land of Russell Management as lessee.

Submissions

[16] Mr Shackleton focused on s 269(3) of the Companies Act, and submitted that the rights of Russell Management as a lessee could not be treated as affected by the disclaimer. He submitted that there was a real question as to whether the liquidator's power under s 269 was exercised, and that a liquidator may only disclaim onerous property and that the leases could not be properly regarded as onerous property. There was an income flow from them and Mr Ronald of Russell Management had sworn an affidavit exhibiting projected figures which showed profitable months to come. However, there was no comment to a statement in the liquidator's first six month's report of 4 December 2008 that there were considerable arrears by Russell

Management in payments for territorial authority water rates and body corporate levies, marketing costs and costs of operating the units as serviced apartments. The liquidator stated in that report that the contract was unprofitable and a property of the company which was unsaleable or not readily saleable and which might give rise to a liability to pay money to perform an onerous act.

[17] It is to be noted that Russell Management did not take any steps to apply to reverse or modify the disclaimer. Apart from sending two letters it did nothing about the disclaimer until 2 December 2008, by which time it was aware that the agreement to sell the property had been signed. Mr Shackleton has given no explanation as to why this step has not been taken. I note that Mr Shackleton has only been instructed in the last few days.

Does the disclaimer terminate the lease?

[18] It is necessary to turn first to the words of s 269(3). The disclaimer under the section brings to an end on and from the date of the disclaimer the "rights, interests and liabilities of the company" in relation to the property disclaimed, in this case the lease. Section 269(3)(b) states, however, that it does not "except so far as necessary to release the company from a liability" affect the rights and liabilities of any other person.

[19] There is no doubt that an owner of a reversion has rights, interests and liabilities. Lord Nichols observed in considering a disclaimer of a lessee's interest in *Hindcastle Ltd v Barbara Attenborough Associates Ltd* [1997] AC 70 (HL), under the then equivalent United Kingdom legislation, at 87:

> In order to determine these rights and obligations it is necessary, in the nature of things, that the landlord's obligations and rights, which are the reverse side of the tenant's rights and obligations, must also be determined. If the tenant's liabilities to the landlord are to be extinguished, of necessity so also must be the landlord's rights against the tenant. The one cannot be achieved without the other.

In setting out the "rights" of the lessor Lord Nicholls referred to the right to be paid rent. In respect of the liabilities of the lessor he referred to the obligation of a lessor to afford to the lessee quiet enjoyment. The statements were made in the context of

a disclaimer of a liquidator of a lessee. Such disclaimers are common. That is not the case with a disclaimer by a lessor.

[20] While undoubtedly those contractual elements in a lease from a lessor's perspective are rights and liabilities within the words of s 269(3), that section makes no reference to a disclaimer being sufficient to terminate an interest in the land. The subject matter of the disclaimer here is not just a contract. It is a leasehold estate in land. This is different from a disclaimer by the liquidator of a lessee, where the lessor's interest in the land continues, and only the lease is lost. What the liquidator of Winslow seeks to do is to divest Russell Management as lessee of an interest in the land.

[21] I am informed that some of the leases have been registered and it is possible that these leases are capable of registration. That is not a matter on which I have heard submissions, but in any event there is no doubt that the leases created an interest in the land.

[22] It is also to be noted that what can be disclaimed is only that which is necessary to release the company from liabilities and is not, save as is necessary, to affect the rights or liabilities of any other person. Russell Management undoubtedly has a right as lessee. There must be a question as to whether its rights and liabilities can be preserved.

[23] The issue of the right to disclaim in relation to interests in land has been considered in a number of cases. In *Re Bastable, ex parte The Trustee* [1901] 2 KB 518 (CA), a trustee in bankruptcy sought to disclaim a contract entered into by the bankrupt for the sale of a lease. Collins LJ commented in relation to the right to disclaim, at p 526:

> But the matter does not rest there, because the subject matter of the sale in this case is real estate, and such a contract of sale, whether followed or not by payment of a deposit, operates to pass to the purchaser an equitable interest in the land, and the effect of a disclaimer of the contract now would be not to relieve the trustee from a burden, but to divest and take out of the purchaser the property which is already vested in him. No doubt the section might have so provided; but is there anything in it even to suggest that it has so enacted?

And later at 527:

> It does not appear to me that this disclaimer section operates to alter those rights, or to give to the trustee a right to take out of a person an equitable interest which has passed to him by contract from the bankrupt, and thus to stand free of the equity already created by the bankrupt.

Romer LJ noted that the purchaser of the lease had an equitable interest in the land itself. He observed at 528:

> That interest in the land would remain whatever might be the effect of a disclaimer by the trustee in the vendor's bankruptcy of the contract for sale.

[24] This case arose in the context of a bankruptcy, but the English legislation that applied appeared to follow in a general way the wording that is referred to in s 269(3). *Re Bastable, ex parte The Trustee* related to an agreement for sale and purchase of a leasehold interest, but the equitable interest referred to was that of the purchaser of a leasehold interest. It was the leasehold interest that was the basis for the claimed equitable interest. *Re Bastable, ex parte The Trustee* has certainly been interpreted as standing for the proposition that a disclaimer cannot divest any equitable interest that a person may have in land: *Dekala Pty Ltd (In Liquidation) v Perth Land & Leisure Ltd* (1988) 6 ACLC 131 at 133. However, in some English cases disclaimers that appear to have effected some equitable interests in land have been held to be effective: *Re Maughan, ex parte Monkhouse* (1885) 14 QBD 956.

[25] In the case of *Re Gough, Hanning v Lowe* (1927) 96 LJ Ch 239, it was observed at 240 that a trustee in bankruptcy could not disclaim so as to deprive a third party of an equitable right vested in that third party before the bankruptcy.

[26] In *Re AE Realisations (1985) Ltd* [1987] 3 All ER 83, a case relied on by Mr Barker for Capital, it was held that a disclaimer destroyed an underlease. It was observed at 91 that "The determination of the bankrupt's rights, interests and liabilities necessarily involved the extinction of his liability under the underlease…". Nevertheless, it was held that the underlessee was entitled to remain in possession so long as the lease, apart from any forfeiture, would have remained in existence. The facts of that case were complex and different from the present.

[27] The case law was reviewed in the New Zealand decision of *Re Richmond Commercial Developments Ltd* (1990) 5 NZCLC 66,336. In that case Wallace J considered in some detail the decision of *Re Bastable, ex parte The Trustee*. He also referred to *Dekala Pty Ltd (In Liquidation) v Perth Land & Leisure* and *Re Hanning v Lowe*. He stated at p 7:

> I am inclined to accept that normally the statutory manager or liquidator of a lessor will not be able to disclaim a lease and indeed I have not been referred to any case in which a liquidator of a lessor has attempted to do so (though that is hardly surprising because normally the lease will be beneficial to the lessor). In relation to disclaimer by a lessor there may on occasions also be issues to consider concerning the Land Transfer Act 1952, though no submissions were made to me in that regard in the present case.
>
> While, however, disclaimer by a lessor may not normally be permissible, there may be instances, and I incline to the view (depending on all the evidence ultimately produced) that the present case is one, when an agreement by a lessor to lease a property falls squarely into the category of an unprofitable contract.

[28] Wallace J distinguished *Re Bastable, ex parte The Trustee* on the basis that the agreement to lease before him fell within the category of an unprofitable contract, which was not the case in *Re Bastable, ex parte The Trustee*. He also noted that in the case before him there might be no third party whose rights were affected if the agreement to lease was disclaimed. He noted that the issue as to the effect of the disclaimer turned on the facts and that exceptional circumstances might also be relevant. He quoted from McDonald, Henry & Meek *Australian Bankruptcy Law and Practice* (5ed 1996) at p 351:

> It would seem inconceivable that the Court would allow a trustee by a disclaimer to take away from a purchaser of land from a bankrupt the equitable interest which vested in him under the contract (*Re Bastable, ex parte The Trustee* [1901] 2 KB 518 (CA) except, perhaps in exceptional circumstances.

[29] Wallace J did not determine the issue and gave only an interim judgment. There was insufficient evidence before him to enable a decision to be reached. Clearly, however, he had the preliminary view that while a disclaimer by a lessor might not normally be permissible there might be instances where an agreement for lease could come into the category of an unprofitable contract.

[30] Some of the cases referred to, *Re Gough*, *Hanning v Lowe*, *Re Bastable, ex parte The Trustee*, *Dekala Pty Ltd (In Liquidation) v Perth Land & Leisure Ltd*, indicate that a disclaimer cannot operate as a termination of the lease. The analysis of Wallace J in *Re Richmond Commercial Developments Ltd* deserves great respect and it may be that in a substantive hearing of a s 284 application, a disclaimer of the lease could be upheld.

[31] What is clear, however, is that Russell Management has an arguable claim for an ongoing interest in the land as lessee. The disclaimer may not have effectively brought the lease, and Russell Management's interest in the land, to an end.

[32] While there has been some delay on Russell Management's part, I do not consider it to be significant enough to prompt any exercise of the wider discretion the court may have to refuse to allow the caveat to stay on the title. It is surprising that Russell Management has not applied under s 284, but it did send letters setting out its position early on and it has been explained in an affidavit that it had hoped to resolve matters by negotiation.

[33] It is to be noted that Winslow had the option of disclaiming its ownership of the land itself. It has chosen not to do so and only disclaimed the lease. Just as there is a question as to whether the delay in Russell Management taking any formal steps might have had a tactical basis, the question also arises as to why the liquidator has disclaimed only the lease and not the land itself.

[34] Irrespective of issues of whether an interest in the land can be disclaimed there is clearly a serious question as to whether it can be said that the lease was onerous property, and in particular as to whether it was unprofitable in terms of s 269(2). Russell Management should have the opportunity to challenge Winslow's disclaimer. However, it must do so promptly.

[35] Both Mr Barker for Capital and Mr Shackleton for Russell Management agree that this should be an interim judgment only in relation to the caveat. This is because Capital will argue that any interest that Russell Management has in the land is of a lower priority than Capital's interest. It is asserted that Capital's mortgage

interest was prior in time to the Russell Management leases. Mr Barker wishes to have that point preserved for further argument if necessary. He has not pursued it during this hearing because of the urgency and the constraints on time.

[36] I observe that it seems likely that there may be disputed matters of fact in relation to this issue of priorities. If that is so, the matter may be better progressed by substantive proceedings where a declaration is sought determining the issue. Nevertheless, I accede to counsel's request. This is an interim judgment only.

[37] I make the following orders and directions.

a) The application to remove Caveat 8014923.1 on the basis that the disclaimer terminated Russell Management's interest in the land is declined. The application is not, however, finally determined and it is open to Capital to pursue its application on the ground that Capital's mortgage has priority over any interest of Russell Management.

b) Russell Management is to make application under s 284 for an order reversing or modifying the disclaimer of Winslow of 29 August 2008, on or before Monday, 19 January 2009.

Costs

[38] Costs are reserved. Given the interim nature of this decision it is not appropriate to finally determine that issue at this point.

…….

Asher J