IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY

I TE KŌTI MATUA O AOTEAROA
TE WHANGANUI-A-TARA ROHE

CIV-2018-485-792
[2018] NZHC 2934

UNDER	the Receiverships Act 1993 and Part 19 of the High Court Rules 2016
BETWEEN	LARA MAREE BENNETT, JOHN HOWARD FISK and MICHAEL LONGMAN Applicants
AND	EBERT CONSTRUCTION LIMITED (in receivership and liquidation) Respondent
	AUCKLAND VENTILATION SERVICES LTD First Interested Party
	TASLO STEEL SECURITY LIMITED Second Interested Party

Hearing:	8 November 2018
Counsel:	M G Colson and R L Pinny for the Applicants C R Andrews for First Interested Party K Badcock for Second Interested Party
Judgment:	12 November 2018

JUDGMENT OF CHURCHMAN J

Introduction

[1] On 31 July 2018, the Bank of New Zealand, exercising their power under a General Security Agreement (GSA) appointed the applicants receivers of the respondent.

[2] On 3 October 2018, David Ruscoe and Timothy Downes (the Liquidators) were appointed by the shareholders as liquidators of the respondent.

[3] Up until it was placed into receivership, the respondent was a substantial construction company with 15 active project sites throughout the country and a staff of approximately 100. It had forecast turnover for the year to 31 March 2019 of $171 million. It had engaged over 150 subcontractors, some of whom worked on multiple projects.

[4] The Construction Contracts Act 2002 (the Act) provided that, in relation to commercial construction contracts (CCCs) entered into after 31 March 2017, a head contractor (such as the respondent) withholding sums which would otherwise be required to be paid to a subcontractor (retentions), must hold those funds on trust for the subcontractor.

[5] As at the date of the receivership, the respondent had a Retention Account for retentions covered by the Act with a balance of $3,678,832.53.

[6] Upon receivership, the respondent owed its trade creditors (including subcontractors) approximately $24.517 million (including GST) and a further $9.324 million (excluding GST) in subcontractor retentions. The $3.678 million held in the Retention Account represents the respondent's only significant cash asset. There is likely to be a significant shortfall in the respondent's insolvency. This means that, other than any payment that they may receive from the Retention Account, the subcontractors are most unlikely to receive any other payments in relation to the monies owed to them by the respondent.

[7] There are some 152 subcontractors who could potentially have a claim against the funds in the Retention Account and these claims arise from some 213 separate CCCs.

The issues

[8] This application relates to how the funds held in the Retention Account should be distributed. For various reasons which will be addressed in detail later, the funds

held in the Retention Account are insufficient to satisfy the claims of all 152 potentially affected subcontractors.

[9] The claims of some 131 subcontractors are clear and not contentious. There is uncertainty in relation to some 21 of the claims. For those 21 subcontractors, the conclusion I come to, will determine whether they receive anything at all from the Retention Account. For the 131 subcontractors, the decision that I will come to will result in a fractional adjustment to the funds that they are likely to receive.

The parties

[10] The applicants are the receivers of the respondent. However, unless appointed by the Court, they would not be the receivers of the Retention Account. That is because those funds (with a possible exception of interest earned on them) are not the property of the respondent. They are held on trust for the qualifying subcontractors.

[11] Unless someone applies to be the receivers and managers of the Retention Account, nothing will happen to those funds. The applicants appreciate that this would be most unfortunate for the subcontractors, all of whom have already lost significant sums of money as a result of the collapse of the respondent.

[12] Responsibly, they have therefore made application to be appointed receivers and managers of the fund and for a direction that their fees be paid out of that fund.

[13] The liquidators are not parties to these proceedings but have formally indicated that they support the application.

[14] In accordance with directions made by Associate Judge Johnston in a minute of 26 October 2018, all parties potentially affected by the application were served. The directions made by Associate Judge Johnston gave any party who wished to join the proceeding until Thursday 1 November 2018 to apply to do so.

[15] Two subcontractors have responded after being served.

[16] Kevin Badcock acting for Taslo Steel Security Limited (Taslo) filed a memorandum on 2 November 2018 indicating that it did not oppose the application in principle but raised concerns about some aspects of it.

[17] The concerns related to the claimed haste with which the application proceeded and the provision for the costs of the applicants to be paid from the fund.

[18] The memorandum said that Taslo was owed approximately $500,000 by the respondent in relation to unpaid progress payment claims and outstanding retentions and was one of the top 12 subcontractors who had an entitlement to the fund. It was said that the amounts owed from the fund to the top 12 subcontractors made up some 47 percent of the fund. The memorandum noted that Taslo had initially offered to financially support an application by the applicants for the types of orders sought in this application but that because of insufficient offers of financial support from other subcontractors, the initial proposal was not pursued and consequently the only funds available to support the application were those in the fund itself.

[19] The other significant concern expressed on behalf of Taslo was its claim:

> … that the Applicants were attempting to obtain Orders to use the Fund to cover costs/fees that the Receiver/Liquidator would in any event ordinarily have to occur and the receivership/liquidation so as to determine how much each creditor was owed.

[20] The memorandum contained an acknowledgement that the anticipated receivers' costs of $150,000 excluding GST and disbursements "does not appear to be unreasonable in the circumstances".

[21] Taslo wanted the receivers' costs to be kept at $150,000 and that:

> Should the Applicants require further funding, the Applicants can be granted leave to make a further application to the Court which sensibly would need to be on notice to all Subcontractors and Principals.

[22] A memorandum was also received from another subcontractor, Auckland Ventilation Services Limited (AVSL) and Mr Andrews appeared on their behalf and made submissions at the hearing.

[23] The memorandum was generally supportive of the application and indicated that AVSL was an affected subcontractor who was a party to some seven subcontracts entered into on or after 1 April 2017 in respect of which retentions had or ought to have been transferred and held on trust.

[24] The significance of 1 April 2017 is that is the date on which the provisions of the Act came into effect that required the respondent to hold retentions on trust. Retentions in relation to contracts entered into prior to that date had been deducted by the respondent but it had not been obliged to hold them on trust and they had been held in the firm's general account and therefore had ceased to exist given the absence of funds in that account as at the date of the receivership.

[25] The memorandum recorded that AVSL had formally cancelled each of its seven subcontracts with the respondent on the grounds that the respondent had committed an act of insolvency and believed that it was entitled to immediate distribution of its share of the funds without any deduction for alleged default.

[26] A separate memorandum of counsel dated 6 November 2018 noted that AVSL's claims against the fund represented approximately 14.8 per cent of the Reconciled and Transferred Retention fund.

[27] AVSL did not support Taslo's submission that the Court should impose a cap on the applicants' costs. It supported the proposal advanced by the applicants that they be required to submit a final report to the Court on costs and that those costs should be approved by the Court before being deducted. It was submitted that the costs report should be served on all other parties who have filed appearances in the proceeding and that they be given an opportunity to make submissions, on the papers, if necessary, in order to keep the costs down.

[28] AVSL sought a reservation of leave to all parties to seek further directions on short notice. It indicated that it would abide the Court's decision on categorisation and acceptance of claims by differently affected subcontractors.

[29] AVSL abided the decision of the Court in respect to a *pari passu* distribution now, with accrued interest agglomerated into the fund and the receivers' costs for management and administration of the fund, including the current application to be payable from the fund.

Relevant facts

[30] The respondent used an industry standard form of subcontract known as SA2009. The contracts provided for the respondent to hold retentions. The retentions were generally 10 per cent of the sums due.

[31] Retentions were generally released in two stages with the first release being on Practical Completion or Taking Over (usually 50 per cent) and the second release being at the expiry of the defects liability period in the head contract. The defects liability period was usually 52 weeks from the date of Practical Completion.

[32] The due date for initial retention release (50 per cent) was 22 working days after the end of the month in which the practical completion certificate was issued. The due date for final retention release was 25 working days after issue of the defects liability certificate under the Head Contract or seven working days after completion of maintenance or rectification of all defects in the subcontract works, whichever is later.

[33] Essentially the purpose of retentions was to ensure that work was carried out by the subcontractor to the appropriate standard.

The mechanism for approval and payment

[34] In practice, a subcontractor would submit a payment claim and the respondent would then consider whether the claim was in accordance with what it considered was owing under the CCC. Once it had determined how much it considered it was payable under the CCC, the respondent created a buyer created tax invoice (BCTI) which recorded the amount to be paid to the subcontractor and the amount which was being retained. The respondent would send the BCTIs to the subcontractors and pay the amounts due and owing under the BCTIs to the subcontractor from its general account.

[35] Deductions in respect of retention for contracts entered into prior to 31 March 2017 were made from the payments made to the subcontractor, but the deductions remained in the respondent's general account.

[36] For CCCs which were treated by the respondent as entered into after 31 March 2017, once the BCTIs were processed, the respondent would carry out a monthly reconciliation process for retentions which were required to be held on trust.

[37] In undertaking the monthly reconciliation process, the respondent would determine the net movement in retentions subject to the Act comprising:

(a) the quantum of the new retentions being held for that month's invoices; and

(b) from the retentions already withheld and reconciled to the Retention Account, the amounts which were to be released from trust under the terms of the relevant CCC and the Act through either:

(i) payment to the subcontractor; or

(ii) transfer back into the respondent's general account as amounts it was entitled to deduct from the retention in respect of defaults by the subcontractor.

[38] The respondent then ran an accounting software programme called CHEOPS over the transactions. If the net movement of funds was positive, funds comprising the net movement would be transferred from the respondent's general account to the Retention Account. If the net movement was negative, funds comprising the net movement would be transferred from the Retention Account into the general account.

[39] Provided the CCCs entered into the respondent's system were correctly coded as to whether they related to CCCs entered into after or before 31 March 2017, and the reconciliations and transfers completed, the Retention Account would contain the funds required to be held in trust pursuant to the Act.

[40] In the months of June and July 2018, the respondent's systems for reconciling and transferring retentions started to break down. That failure led to three of the four contentious categories of retentions.

Contentious categories

May claims

[41] The respondent followed its usual processes up to 22 June 2018 in respect of claims made by subcontractors in May for work completed up to, and including, May.

[42] The last transfer of retention payments from the respondent's general account to the Retention Account was on 22 June 2018. On that day, $332,680.58 (being the net retention movement for the month to 31 May 2018) was transferred from the respondent's general account to the Retention Account. After that transfer, the amounts in the Retention Account comprised retentions held and reconciled by the respondent up to the end of May 2018 (the Reconciled and Transferred Retentions). The Reconciled and Transferred Retentions totalled $3,678,832.53 and relate to 131 subcontractors in respect of 182 CCCs on 19 projects.

June claims

[43] The respondent did not complete the usual process in respect of claims made by subcontractors in June 2018 for work completed up to, and including June 2018.

[44] During July 2018, the respondent had determined how much it considered was payable under the CCCs for such claims and had created the requisite BCTIs. The June BCTIs recorded the amount to be paid to the subcontractor and the amount which was being retained in the customary way. However:

(a) the amounts payable to the subcontractor under the June BCTIs were (in most cases) not paid; and

(b) no amounts were transferred from the general account to the Retention Account in respect of these retentions (Calculated but Not Transferred Retentions).

[45] The amount of Calculated but Not Transferred Retentions is approximately $475,000. These amounts relate to 80 subcontractors in respect of 97 CCCs for 12 projects.

July claims

[46] The respondent did not complete the usual process in respect of claims made by subcontractors in July 2018 for work completed up to, and including, July 2018. In other words, the respondent did not do any of:

(a) complete the assessment of all claims and issue the BCTIs for services provided by its subcontractors in July 2018;

(b) pay amounts to associated subcontractors in respect of those services;

(c) calculate the confirmed retentions in respect of those services;

(d) pay monies into the Retention Account relating to services provided by the subcontractors in July 2018 (the Uncalculated and Not Transferred Retentions).

[47] These Uncalculated and Not Transferred Retentions have subsequently been calculated to be $380,000 and relate to 70 subcontractors in respect of 83 CCCs for 12 projects.

"Released" but not paid retentions

[48] The respondent did not pay to the subcontractors any amounts in respect of released retentions in relation to CCCs entered into on or after 31 March 2017 in respect of work untaken in June or July 2018.

[49] The respondent:

(a) calculated such amounts to 30 June 2018;

(b) recorded them as Released Retentions in its financial accounts up to 30 June 2018, but no amounts were in fact:

(i) transferred out of the Retention Account in respect of those Released Retentions; or

(ii) paid to the subcontractors concerned. They were recorded in the respondent's system as part of unpaid BCTIs.

[50] The total Released but Not Paid Retentions in respect of June and July 2018 is $68,901.95 owing to four subcontractors which are still held in the Retention Account.

State of the accounts

[51] The respondent's financial accounts recorded "Retentions Held" as being $9,324,209.17 (excluding GST). This represented all amounts the respondent was supposed to be holding as retentions as at 31 July 2018. However, this amount was not represented by cash held either in the Retention Account or anywhere else.

[52] $4,858,137.88 of retentions were not subject to the Act's retentions regime because they related to CCCs entered into before 31 March 2017.

[53] Of the $4,466,071.29 of retentions held in respect of CCCs which were entered into on or after 31 March 2017:

(a) $3,609,930.58 reflects the Reconciled and Transferred Retentions less the unpaid Released Retentions;

(b) approximately $475,000 is the Calculated but Not Transferred Retentions; and

(c) approximately $380,000 is the Uncalculated and Not Transferred Retentions.

[54] However, this figure does not include:

(a) those retentions totalling $68,901.95 which were calculated by the respondent to be the Released Retentions in respect of four subcontractors as at 31 July 2018 but which the respondent had not made any payment in respect of:

(b) retentions of $170,340.39 relating to the Wrongly Classified Subcontracts.

Wrongly Classified Subcontracts

[55] The applicants have identified 14 contracts where the respondent had failed to record in its computer system that the contract was entered into after 31 March 2017. The CHEOPS accounting programme therefore did not recognise the contracts as being subject to the regime of the Act, and no amounts representing retentions under these subcontracts were reconciled with the Retention Account or paid into that account.

[56] As at 31 July 2018, the retentions which should have been reconciled and transferred to the Retention Account in respect of the 14 Wrongly Classified Subcontracts, totalled $170,340.39.

[57] It is clear that there is insufficient in the Retention Account to pay all the 152 subcontractors who potentially have claims to it.

[58] The applicants have sought authority to pay claims on a *pari passu* basis to 75 per cent pending resolution of the contentious claims. They anticipate that it may be possible to make distributions of between $1.4 million and $2 million prior to Christmas.

[59] They also seek the power to make interim distributions for reasons to do with GST. From the information in the second affidavit of Lara Maree Bennett dated 1 November 2018, it is clear that there are significant potential GST advantages in the making of interim payments.

The Act

[60] The retentions scheme implemented by the Act effective from 31 March 2017 was a response to the collapse of the Mainzeal Group in 2013. That collapse had seen subcontractors miss out on retentions totalling $18 million. There was a concern that head contractors were effectively using subcontractors' retentions as working capital and that, on the collapse of a head contractor, subcontractors merely became unsecured creditors, often receiving nothing.

[61] The initial Construction Contracts Amendment Bill was introduced in January 2013 prior to the Mainzeal collapse, but the changes to the retentions regime were introduced to address the issue of retentions and provides some measure of protection to subcontractors.[1]

[62] Although, at the committee stage, the then Minister for Building and Housing, the Hon Dr Nick Smith, said that the effect of the intended legislation was that the retention funds "… are deemed to be held in trust …", it does not seem that the provisions in the legislation actually created a deemed trust. Rather, they created an obligation for the head contractor to hold the retention monies on trust for the affected subcontractors. One difference between the regime proposed and the normal concept of a trust or deemed trust is that the actual retention funds did not have to be retained as cash. As Dr Nick Smith then Minister for Building and Housing said:[2]

> Retentions are to be held on trust. Payers can hold those retentions in liquid assets such as accounts receivables, but if they do not get paid they are still obliged to meet those payments. The trust ends when the retentions are either paid out in full or used to fix defective work.

[63] Section 5(1) of the Interpretation Act 1999 requires the Court to ascertain the meaning of an enactment by reference to its text and in light of its purpose. While it is clear that the purpose of the Act relating to retentions was to provide a greater security for subcontracts than existed previously, there were gaps in the legislation and the language used was imprecise.

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1 See Parliamentary Debates 703 NZPD 2243 (12 March 2015).
2 709 NZPD 7347 (20 October 2015).

[64] However, there are some definitions which are of assistance in addressing the issues raised in this case.

"Retention money"

[65] For the purposes of the Act "retention money" was defined in s 18A as:

> … an amount withheld by the party to a construction contract (**Party A**) from an amount payable to another party to the contract (**Party B**) as security for the performance of Party B's obligations under the contract.

[66] When analysed in terms of contract law, a retention is an agreed conditional deferral of part of a *chose in action* (i.e. a debt). Under the Act, "retention money" does not equate to cash in the bank.

[67] The core obligation to hold retention money on trust is set out in s 18C of the Act:

> **18C Default arrangement: Trust Over Retention Money**
>
> (1) All retention money must be held on trust by Party A as trustee, for the benefit of Party B.
>
> (i) However, see section 18D (which allows for an alternative arrangement, involving a complying instrument, to protect the payment to Party B if Party A fails to pay).
>
> (2) Retention money held on trust may be held in the form of cash or other liquid assets that are readily converted into cash.
>
> (3) A trust over retention money ends when–
>
> (a) the money is paid to Party B; or
>
> (b) a Party B, in writing, agrees to give up any claim to the money; or
>
> (c) the money seizes to be payable to Party B under the contract or otherwise by operation of law.

[68] The scheme then is that Party A must hold on trust, some property equivalent in value to the retention money or make some approved arrangement with a third party within s 18D such as a third party bond or letter of credit.

[69] Given the sums of money involved, it seems inherently improbable that the reference to "cash" in s 18C was intended to refer to bank notes.

[70] There is a critical restriction on the use to which Party A can put Retention Money. Section 18E provides:

> **Section 18E Use of Retention Money**
>
> (1) Party B must not appropriate any retention money held on trust to a use other than to remedy defects in the performance of Party B's obligations under the contract.

[71] Unlike what might be expected with more conventional trust arrangements, there is no need for Party A to hold retention monies for Party B in a separate account, and they may be co-mingled with other monies.[3]

[72] In a further departure from conventional trust principles, s 18F also permits Party A to invest the retention monies. It provides that if this investment results in a loss then Party A must make up the difference of that loss; but if the reverse occurs, then Party B may keep the profit.

[73] The entitlement of Party A to keep the interest on retention funds and any profit generated by their investment is a major departure from equitable trust principles and, on the facts of this case, presents some problems as to the entitlement to any interest on the monies in the retention account when the fact that the interest has accrued is, in large part, due to the failure by the respondent to pay the monies out when due.

[74] It is clear from ss 18C, 18E, 18F, and 18FB that Party A has a range of alternatives, and considerable flexibility, as to how it satisfies its obligations to hold on trust an amount of liquid assets equivalent to the amount of the retention monies.

[75] Another unusual provision is that s 18FC provides "audit rights" for Party B in respect of the property held on trust.

[76] Section 18FC obliges Party A to keep proper accounting records of:

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[3] See s 18E(2).

(i) all retention monies held on trust; and

(ii) all amounts of retention money protected by instruments issued for the purpose of this subpart; and

(iii) all dealings and transactions in relation to retention money or instruments.

[77] Section 18FC(4) obliged Party A to make the accounting and other records available for inspection by Party B at all reasonable times and without charge.

[78] If the legislature's intent had been to deem Party A's assets to be held on trust up to the amount of the retention money, it is hard to see why an audit right of this type would be necessary.

[79] Section 18FA of the Act gives retention monies a protection which is relevant to the issues the Court has to determine in this case. The section provides:

Protection of retention money

Retention money held on trust–

(a) Is not available for the payment of debts of any creditor of Party A (other than Party B);

(b) Is not liable to be attached or taken in execution under the order or process of any Court at the instance of any creditor of Party A (other than Party B).

Legal issues

[80] There are three main legal issues in this case:

(a) Whether the Applicants should be appointed by the Court as receivers to manage and distribute the Fund.

(b) Which subcontractors have a claim to the Fund and on what basis.

(c) How to distribute the Fund if, as expected, there is a shortfall.

Appointment of applicants

Need for an order

[81] The first question to be addressed is whether or not the applicants, being receivers appointed pursuant to a general security agreement, would be entitled to administer the retention fund without the Court making an order to that effect. One argument in favour of that proposition is that legal title to the fund is held by the respondent.

[82] However, there is a contrary argument based on the fact that the equitable ownership of the retention monies in the fund is clearly held by the subcontractors. In circumstances where the fund holder is in default of its obligations to the subcontractors, there is obviously a question as to whether any interest earned on the fund is also held for the benefit of the subcontractors, at least from the date of the respondent's default.

[83] There is also potentially a conflict of interest. Section 18(1) of the Receiverships Act 1993 requires receivers to exercise their powers for a proper purpose or in a manner in which they believe on reasonable grounds to be in the best interests of the person in whose interest they were appointed.

[84] Given that the equitable ownership of the fund lies with the subcontractors, it is difficult to see what interest the secured creditor has in the fund. It is possible that there may have been defaults by some of the subcontractors which might have entitled the respondent to retain some or all of the retentions money. Arguably, the respondent may have some entitlement to those funds. However, in circumstances where, as a direct result of the respondent's default, there are insufficient funds in the Retention Account to cover all of the monies that the respondent was obliged, under the Act, to hold in that account, it would be unconscionable for the respondent to assert ownership of such funds at the expense of the general pool of subcontractors.

[85] There is no doubt that a receiver abuses his or her powers by exercising them other than for the purpose of enabling the assets subject to the security to be preserved and realised. The High Court applied this principle in *Downsview Nominees Ltd v*

Official Assignee holding that the receiver had breached his obligations in going well beyond the limited purposes from which a receiver is authorised to act.[4]

[86] A further practical impediment to the applicants being entitled to manage the retention fund without an order from the Court appointing them to do that would be that the receivers would be unable to deduct their costs in managing and distributing the fund from the fund itself.

[87] Section 18E of the Act does not authorise Party A (or receivers acting on behalf of Party A) to appropriate:[5]

> … any retention money held on trust to a use other than to remedy defects in the performance of Party B's obligations under the contract.

[88] Section 18I(1)(c) stipulates that any term in a construction contract is void that purports to require Party B to pay any fees or costs for administering a trust or an instrument under this subpart.

[89] Understandably, receivers such as the applicants, would be reluctant to assume an obligation of managing and distributing a retention fund if they were no under no legal obligation to do so and could not lawfully recover the costs entailed.

[90] In the present case, there is also a further factual complication. The Court was advised that there is a real prospect that the receivership may come to an end before the distribution of the funds is completed. If another party such as the liquidators were obliged then to step in and to complete the work commenced by the receivers in relation to the retention fund, there would be a duplication of cost and also delay.

[91] The liquidators would be faced with exactly the same uncertainty as to their powers in respect of the administration of the fund as the receivers are.

[92] The High Court has an inherent power to appoint a receiver. As Katz J noted in *Rea v Omana Ranch Ltd*:[6]

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4 *Downsview Nominees Ltd v Official Assignee* (1994) 7 NZCLC 260, 605.
5 Section 18E(i) Construction Contracts Act 2002.
6 *Rea v Omana Ranch Ltd* [2013] 1 NZLR 587 at [7].

> The Court's power to appoint a receiver as part of its auxiliary equitable jurisdiction dates back to at least the 16th Century. It was described in *Hopkins v Worcester & Birmingham Canal Proprietors* as one of the oldest remedies in the Court of Chancery. (citation omitted)

[93] In New Zealand, the Court's power to appoint receiver derives from its inherent jurisdiction as preserved by s 12 of the Senior Courts Act 2016.

[94] The jurisdiction to appoint receivers vested in the High Court has been held to be the law as administered in the Court of Chancery in England prior to the enactment of the Supreme Court of Judicature Act 1873 (UK).[7]

[95] Receivers have historically been appointed by the Court in its equitable jurisdiction where:

(a) there was a need for the interim protection of property including disputes about partnerships or the administration of estates; and

(b) to facilitate the execution of judgments where no remedy was otherwise open to the entitled party.

[96] In *Rea v Omana Ranch Ltd*, the Court said:[8]

> Court-appointed receivers are officers of the Court. They are answerable to the Court alone and are not controlled by either the grantor or its creditors…. The Court retains the right to review and control the receiver's conduct.

[97] In *Rea v Omana Ranch Ltd*[9], Katz J summarised the English authority on remuneration of Court-appointed receivers and concluded:[10]

> The proposition that a Court-appointed receiver is entitled to his or her remuneration, costs and expenses out of the receivership assets is therefore the necessary starting point.

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7 *Evans v Robertson Orr* [1923] NZLR 769; *Murtagh v Murtagh* [1960] NZLR 890 and *Vuletic v Vuletic* HC Auckland CP 13228/88, 28 July 1988.

8 Above n 6, at [11].

9 At [12]-[13].

10 At [14].

[98] One factor which has previously been relevant in convincing the Court to exercise its inherent jurisdiction to appoint a receiver, is whether or not anyone is actually managing the fund in question.

[99] In *Te Runanganui o Ngāti Kahungunu Inc v Scott*[11] quoted with approval a passage from *Owen v Homan*[12] which had been referred to by Barker J in *Re Samco Sargent Consolidated Ltd*[13] where the Lord Chancellor had said:

> No one is in the actual lawful enjoyment of the property so circumstanced, and no wrong can be done to any one by taking and preserving it for the benefit of the successful litigant.

[100] Although Mr Badcock, on behalf of the Second Interested Party, submitted that it appeared that the applicants were attempting to obtain orders to use the fund to cover costs/fees that the receivers/liquidator would in any event ordinarily have to incur in the receivership/liquidation so to determine how much each creditor was owed, I do not accept that there is any substance in that submission.

[101] Mr Colson, for the applicants, stated in his submissions:

> The Applicants have already completed over 100 hours of work in respect of the Fund. To the extent this work overlapped with their duties as GSA receivers it accordingly would be of no cost to the Fund.

[102] For the above reasons, I am satisfied that:

(a) the applicants, as receivers of the respondent, would not, in the absence of a Court order, be entitled to administer the fund;

(b) that the Court has an inherent jurisdiction to appoint receivers and managers of the fund for the purpose of distributing the retention funds and resolving any issues arising from that process;

(c) that as receivers appointed pursuant to the Court's inherent jurisdiction, it is appropriate that their fees and costs are met from the fund.

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11 *Te Runanganui o Ngāti Kahungunu Inc v Scott* [1995] 250, Neazor J.
12 *Owen v Homan* (1853) 4 HL Cas 997.
13 *Re Samco Sargent Consolidated Ltd* (1977) 1 BCR 112 at p 1032.

[103] In respect of the scale of fees set out in [10.6] of Ms Bennett's second affidavit of 1 November 2018, I am satisfied that they are appropriate.

[104] As to whether or not the costs should be capped at $150,000 (as argued for by Taslo), or should be subject to ultimate review by the Court (as sought by the receivers and supported by AVSL), I have come to the conclusion that, consistent with the Court's rights to review the fees and costs by a Court-appointed receiver, it is appropriate that the receivers' ultimate fees and costs are submitted to the Court for review and approval rather than be fixed at this point.

[105] It is appropriate that any of the subcontractors affected by these proceedings (and not just the two interested parties as submitted by AVSL) are entitled to make representations to the Court in respect of the applicants' fees and costs. However, in order to minimise the legal costs that this might generate, it is appropriate that this be done by way of the applicants filing a memorandum detailing the fees and costs, and serving same on all subcontractors in the same manner that Associate Judge Johnston approved for service of the original proceedings.[14]

[106] Any subcontractor wishing to file a memorandum in response shall do so within 14 days of service and the issue shall be resolved on the papers.

[107] I also grant the applicants leave to return to the Court for further directions relating to the distribution of the fund if needed.

The contested claims

[108] The Courts have traditionally required three certainties for the creation of a trust. These are certainties as to:

(a) intention to create a trust;

(b) subject matter of the trusts; and

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[14] *Bennet, Fisk and Longman v Ebert Construction Ltd (in receivership and liquidation)* CIV-2018-485-792 at [5].

(c) object (or beneficiaries) of the trust.[15]

[109] It is clear that the Reconciled and Transferred Retentions meet these requirements. It is also clear that they meet the requirements of the Act. The most critical requirement is arguably that in s 18A which says:

> … unless the context otherwise requires, **retention money** means an amount withheld by a party to a construction contract (**Party A**) from an amount payable to another party to the contract (**Party B**) as security for the performance of Party B's obligation under the contract. (underlining added)

[110] Therefore, the reconciled and transferred retentions are held in the Retention Account in trust for the 131 affected subcontractors.

Calculated but Not Transferred Retentions

[111] Before considering the three certainties, it is necessary to have regard to s 18A of the Act and its definition of "retention money" as being an amount that has been withheld.

[112] The amounts due and owing to most (but not all) subcontractors under the June BCTIs were not paid. Although the respondent calculated the amount to be withheld, (at least in respect of the June BCTIs where no payments were made to the subcontractors), there was nothing "withheld". Where no payments were made, obviously nothing could be said to have been withheld from those payments and, obviously, no monies were paid into the Retention Account.

[113] The respondent simply defaulted on all its legal obligations including its obligations under the Act.

[114] In respect of the few June BCTIs that were paid, if retentions were withheld and if they were deposited into the Retention Account, then those subcontractors would fall into the same category as the Reconciled and Transferred Retentions.

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15 *Butler (ed) Equity and Trusts in New Zealand* (Brookers, Wellington 2009) at 421.

[115] In terms of the three certainties, the respondent cannot be said to have had any intention to place retention monies in trust when it did not make any retention deductions.

[116] There is a further reason, arising out of the wording in the Act itself, which indicates that the monies in the Retention Account are not available to the Calculated but not Transferred Retentions subcontractors. That is a requirement in s 18FA that retention money held on trust:[16]

> … is not available for the payment of debts of any creditor of Party A (other than Party B).

[117] The respondent's accounting records are sufficiently accurate to show exactly which party the funds in the Retention Account are held for. They do not identify any funds held on behalf of a Calculated but not Transferred Retentions category subcontractors.

[118] It may be argued that the intention of the Act was to create a "deemed trust" and, consistently with that intention, even where there had been no retentions deducted because the contractual payments of the BCTIs were not made, the relevant subcontractors still had an equitable interest in the fund.

[119] In spite of the imprecise language used by the framers of the legislation, it is clear that the type of trust created by the Act differs in many important respects from normal trusts. The Act has been prescriptive as to what "retention money" means. Unless there has been a deduction from an amount payable to a subcontractor, no "retention money" has come into existence. Accordingly, those subcontractors who fall within the category of Calculated but not Transferred Retentions, do not have an interest in the funds held in the Retention Account.

Uncalculated and Transferred Retentions

[120] Many of the same arguments that apply to Calculated but not Transferred Retentions apply to Uncalculated and Not Transferred Retentions.

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[16] Section 18FA(a), Construction Contracts Act 2002.

[121] As at the date of the receivers' appointment, the respondent had not completed its reconciliation process for July 2018. It had not paid any amounts to subcontractors or calculated any retentions in respect of services provided in July and it had obviously not paid any monies into the Retention Account.

[122] In those circumstances, the intention to create a trust is absent as are the necessary steps to create "retention money" required by s 18A. The 70 subcontractors within this category therefore do not have any interest in the monies held in the Retention Account.

"Released" but not Paid Retentions

[123] These retentions were reconciled and transferred into the Retention Account and although the respondent undertook the calculations to "release" them, they were never in fact transferred out of the Retention Account, remaining there as at the date of the appointment of the receivers.

[124] Therefore, the three certainties are satisfied as are the requirements of ss 18A and 18FA(b). The subcontractors falling into this category are entitled to share in the Retention Account on the same basis as the other subcontractors who fall into the Reconciled and Transferred Retention subcontractors.

Wrongly classified subcontractors

[125] Although the respondent intended to comply with its obligations to pay into the Retention Account all retentions deducted from payments made in respect of contracts entered into after 31 March 2017, it failed to do so in respect of this category of subcontractor because it either incorrectly recorded the relevant start date of the contract or failed to record any start date thereby not activating the CHEOPS computer programme which calculated what retentions should be transferred into the Retention Account.

[126] It is arguable that the respondent had the intention to hold on trust all retentions which were, in fact, deducted from post-31 March 2017 CCCs, and only failed to do that in respect of these contracts because of its own error.

[127] However, the difficulty for this category of subcontractor is the prohibition in s 18FA(b) limiting the use of funds in the account solely to discharge obligations to the subcontractors from whose payments these funds were deducted.

[128] Although retentions were deducted, they were not transferred into the account.

[129] Although there is no obligation on a head contractor to hold retention funds in a particular bank account or even in cash, unless retentions are transferred into whatever fund or instrument is chosen by the head contractor to represent the value of the retention deductions, the structure of the Act is such that the head contractor is prohibited from using funds which represent deductions made in respect of payments due to Party B in order to satisfy obligations due to Party C.

[130] The unfortunate consequence is that, as a result of the prohibition in s 18E(1) on Party A appropriating any retention money held on trust to a use other than to remedy defects in the performance of Party B's obligation under the contract, the failure by the respondent to correctly classify these contracts and transfer the retentions into the Retention Account mean that the affected subcontractors do not share in the funds in the Retention Account.

Interest

[131] The funds in the Retention Account are presently invested and are earning interests. Pursuant to s 18F(2)(b) and (3) "Party A may retain the benefit of any interest earned on retention money on or before the date on which it is payable under the contract." As mentioned above, there is an argument that the respondent is entitled to the interest.

[132] Equally, there are arguments that the subcontractors are entitled to the interest both in law and in equity.

[133] The retention deductions covered by the fund will be falling due for payment by the respondent to the subcontractors on an ongoing basis. Arguably, as asserted by AVSL, by becoming insolvent, the respondent is in breach of its obligations entitling

the subcontractors to cancel the contracts and demand immediate payment of all retentions.

[134] In those circumstances, there is an argument that, at least from the date of cancellation, if not the date of the demand, the interest belongs to the subcontractor.

[135] I am not required to determine ultimate ownership of interest in these proceedings. However, I sought and obtained from the applicants an undertaking that, pending the further order of the Court, the balance in the Retention Account would not fall below the amount of the interest accrued on that account.

[136] The argument as to entitlement to the interest therefore awaits determination another day.

[137] If the applicants are successful in disbursing between $1.4 million and $2 million prior to Christmas as they have anticipated, the sums involved by way of interest may well be so small that it is uneconomic to litigate ownership and they may be best left to offset, in some small way, the receivers' fees and costs in administering the fund.

[138] In terms of whether interest should be paid to the subcontractors on the retentions, given that there is likely to be a significant shortfall overall, and in view of the relatively modest sums of interest likely to be involved, the pragmatic approach would seem to be to calculate entitlements on the basis of the amount of the original retentions deductions and to ignore any interest component.

[139] Such an approach has the attractive feature of avoiding the complexity and cost of the receivers having to make a number of additional calculations, and also having to obtain an answer from the Court on this issue which will simply further deplete the funds available for distribution. It also avoids the necessity for the delays inherent in the receivers having to ask the Court to clarify this issue.

Outcome

[140] I set out below the outcome:

(a) the applicants are appointed receivers and managers of the Retention Account;

(b) the applicants are entitled to make payments to the subcontractors entitled to share in the Retention Account on a *pari passu* basis and to make interim payments on a basis of 75 per cent of nominal entitlement or such other percentage as seems prudent to the applicants;

(c) the applicants are entitled to deduct their fees, costs and expenses from the fund, and are required to obtain the approval of the Court for their account as detailed above;

(d) the applicants are granted leave to return to the Court for further directions as required;

(e) the two interested parties and any other subcontractor served with these proceedings are entitled to seek further directions from the Court and shall serve any such application on the parties and the other subcontractors in the manner approved in [5] of the minute of Associate Judge Johnston in this matter dated 26 October 2018; and

(f) the applicants are entitled to the costs of this application on an indemnity basis.

[141] I record that the List Judge has now categorised these proceedings as "complex" and directed that I be assigned to case manage these proceedings.

Churchman J

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