IN THE COURT OF APPEAL OF NEW ZEALAND

CA228/2017
[2018] NZCA 15

BETWEEN	COUMAT LIMITED First Appellant
	GREGORY BRUCE HAYHOW Second Appellant
AND	WHITFORD PROPERTIES LIMITED Respondent

Hearing:	14 November 2017
Court:	Asher, Lang and Ellis JJ
Counsel:	P F Dalkie and R Rao for Appellants M C Black for Respondent
Judgment:	16 February 2018 at 10 am

JUDGMENT OF THE COURT

A The application for leave to adduce further evidence is declined.

B The appeal is dismissed.

C The appellants must pay the respondent costs for a standard appeal on a band A basis and usual disbursements.

REASONS OF THE COURT

(Given by Asher J)

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Introduction

[1] This appeal concerns a vendor mortgagee's equitable and statutory duties on a mortgagee sale. In particular, it concerns the duty of a mortgagee to account for a forfeit deposit to the mortgagor, and to account to the mortgagor for any surplus remaining after the amount owing under the mortgage has been repaid.

Facts

[2] The relevant history of the sale begins with the incorporation of the respondent, Whitford Properties Ltd (in liq) (Whitford) on 26 March 2002. Whitford was incorporated by Robert Bruce and Wayne Allen. They were shareholders together with Mr Allen's wife. Shortly afterwards, Whitford acquired a block of land in South Auckland in two titles totalling approximately eight and a half hectares (the Whitford Land). It was then zoned rural but if certain consents could be obtained it could be subdivided for residential purposes. Being close to Auckland it had considerable potential value. The history of the steps taken to get the subdivision underway is complex and does not need to be recited. Of relevance is that on 6 July 2005 a mortgage was registered over the Whitford Land to secure borrowings

by Whitford from ANZ Bank New Zealand Ltd (ANZ).[1] The mortgage was guaranteed by Mr Bruce and Mr Allen.

[3] By April 2014 Whitford was in default on the ANZ mortgage. At that time it owed approximately $8.5 million. Discussions between ANZ and Whitford broke down, and ANZ proceeded to sell the Whitford Land as mortgagee. It adopted a tender process for the sale, and on 16 April 2014 ANZ issued an invitation to tender. The terms of the invitation to tender required the successful tenderer to pay a deposit of 10 per cent of the tendered sum.

[4] By this time the second appellant, Gregory Hayhow, had become involved with Messrs Bruce and Allen. On or about 16 October 2013 he had lent $330,000 to Mr Bruce on the basis of a term loan agreement. The agreement was for a three-month period and featured an interest rate of 400 per cent. As security Mr Hayhow was given a first ranking general security over Mr Bruce's 50 per cent shareholding in Whitford. That security proved to be valueless, because Mr Bruce had already given security over the shares to another party. Therefore, by early 2014 Mr Hayhow had serious concerns about his ability to recover his loan from Mr Bruce.

[5] It seems by early 2014 Messrs Bruce and Allen were no longer working together. Mr Allen wanted to tender in his own name for the Whitford Land in the sum of $9 million. However, unsurprisingly given Whitford's defaults, he lacked sufficient funds to complete a purchase at that price. He approached Mr Hayhow and asked for his financial assistance in making the offer. Mr Hayhow entered into discussions with Mr Allen, and deposed that he did so in order to recoup some of the loan made to Mr Bruce. After some negotiation Mr Hayhow and Mr Allen reached an agreement, documented by a joint venture memorandum dated 10 April 2014. They would establish a limited liability company as a vehicle and there would be a tender offer made on behalf of that entity at a price of $9 million with a deposit of $1 million.

[6] Mr Allen made an initial tender offer of $9 million on 10 April 2014. He increased the offer on 15 April 2014 to $12.5 million (the Initial Tender). On

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[1] Ultimately Whitford's borrowing from ANZ was secured by two mortgages (6485175.2 and 6485203.2).

16 April 2014 ANZ accepted the tender and an agreement was signed (the Initial Tender Agreement). A deposit of $1.25 million was paid. The funds for the deposit were provided by Mr Hayhow. That is a matter to which we will return later in this judgment, as it is central to the appeal.

[7] On or about 8 May 2014 Mr Hayhow incorporated a new company, Whitford Property Developments Ltd (WPDL). He intended this to be the joint venture company, and that he would hold 50 per cent of the shares in that company. On 19 May 2014 his solicitors confirmed to Buddle Findlay, solicitors for ANZ, that WPDL would be nominated as purchaser under the tender for the purchase of the Whitford Land.

[8] Settlement of the Initial Tender Agreement was to take place on Monday 16 June 2014. WPDL was never formally nominated to be the purchaser. Mr Hayhow deposed that by mid-June it became clear that Mr Allen would not be able to provide his share of the funds for the purchase. WPDL was not able to settle on the scheduled day. On 17 June 2014 ANZ served a settlement notice on Mr Allen as the successful tenderer and WPDL as "potential nominee purchaser". The deadline for settlement was Tuesday 24 June 2014. However, Mr Allen was unable to settle by that date. Mr Hayhow now faced the prospect of losing the deposit of $1.25 million that he had paid on behalf of Mr Allen, as well as the $330,000 he had earlier loaned to Mr Bruce.

[9] Mr Hayhow had intense negotiations with ANZ and with Mr Allen's lawyers to try and salvage the position, but nothing came of it. Mr Hayhow deposed that he lost all faith in Mr Allen. Through those days of late June, however, ANZ did not take any steps to cancel the Initial Tender Agreement. Mr Hayhow contacted Mr Bruce to see whether a solution could be reached with him. Mr Bruce was liable as a guarantor of the ANZ mortgage. A proposal was put forward by Mr Bruce's solicitors whereby Mr Bruce would use his guarantee to redeem the Whitford Land for the ANZ mortgage debt, using his rights under the guarantee and ss 97 or 102 of the Property Law Act 2007 (the Act).

[10] On 7 July 2014 Mr Hayhow agreed with Mr Bruce that if Mr Bruce exercised his right as guarantor to redeem the Whitford Land he would provide the necessary money to him on the basis that Mr Hayhow's company, Coumat Ltd (Coumat), the first appellant, would then become the registered proprietor of the Whitford Land. Mr Hayhow is the sole director and shareholder of Coumat. Mr Bruce was prepared to talk to Mr Hayhow, given that he owed an ever-increasing amount of money for his personal loan (increasing at 400 per cent per annum). He also wished to mitigate his liability to ANZ for the $8.5 million still owing, which was accruing interest.

[11] As a result of their discussions Mr Bruce and Mr Hayhow entered into a deed dated 21 July 2014. Mr Bruce was to give notice to ANZ, at Mr Hayhow's request, of his intention to redeem the Whitford Land under ss 97 or 102 of the Act. The mortgage would thereby be transferred to him, enabling him to sell the Whitford Land as mortgagee. Mr Hayhow would provide Mr Bruce with the funds to effect the redemption of the mortgage in consideration for Mr Bruce transferring the Whitford Land to Coumat. Mr Bruce irrevocably appointed Mr Hayhow and his representatives as his attorney. Mr Bruce was to get $100,000 for personal services as project assistant in respect of the subdivision of the Whitford Land. The agreement provided: "Subject to Bruce performing his obligations under this Deed and the Services Contract Hayhow will write off Bruce's debt to him."

[12] A further settlement notice on the Initial Tender Agreement had been issued by ANZ, which was due to expire at 4 pm on 23 July 2014. That afternoon Mr Hayhow met with ANZ and Mr Bruce. They followed an agreed agenda at that meeting, beginning with ANZ formally cancelling the Initial Tender Agreement. A cancellation notice signed on behalf of ANZ was provided whereby ANZ notified Mr Allen as the successful tenderer and WPDL as the potential nominee purchaser that, as a consequence of the failure to settle, the Initial Tender Agreement was cancelled "and the deposit of $1,250,000 is forfeited". The forfeiture of the deposit and its application to Whitford's mortgage was subsequently recorded by ANZ in a settlement statement dated 4 August 2014.

[13] In accordance with the agenda, Mr Bruce then issued a notice to ANZ whereby, pursuant to s 102 of the Act using his rights as guarantor, he redeemed the mortgage.

He gave a notice to ANZ dated 23 July 2014 requesting the transfer of the mortgage to him. The mortgage was so transferred. Mr Bruce and Coumat then entered into a "Private Treaty Agreement" under which Mr Bruce would sell the Whitford Land to Coumat for $7,454,903. That price was calculated on the basis that, at the time, $8,704,902 was owed to ANZ, from which the $1.25 million deposit would be deducted. The Private Treaty Agreement showed the consideration as $7,454,903 with a $1 deposit. The settlement date was 23 July 2014. In addition, Mr Bruce required Mr Hayhow to formally forgive his personal debt.

[14] On 26 July 2014 a "Substitute Private Treaty Agreement" was prepared. This was on the same terms as the earlier Private Treaty Agreement save that the price was stated to be $10,014,956. The deposit was recorded as $2,560,054. This comprised:

(a) $1,310,054, being the extinguishment of Mr Bruce's $330,000 personal debt to Mr Hayhow which had ballooned at the 400 per cent interest rate; and

(b) $1.25 million, being the forfeited deposit paid under the cancelled Initial Tender Agreement. This deposit payment had reduced the ANZ debt from $8,704,902 to $7,454,902.

Interest on the balance of the purchase price was payable at 17 per cent. On 28 July 2014 the Substitute Private Treaty Agreement was signed.

[15] The purchase of the Whitford Land by Coumat from Mr Bruce was settled on 4 August 2014. Coumat was registered as proprietor of the Whitford Land. As per the arrangement between Mr Bruce, Mr Hayhow and Coumat, no funds were paid to Whitford for the Whitford Land. Mr Hayhow's provision of the deposit of $1.25 million under the Initial Tender Agreement, his forgiveness of Mr Bruce's personal debt and his provision of the funds that enabled Mr Bruce to redeem the mortgage as guarantor were treated as payment of the purchase price.

[16] In due course Whitford went into liquidation. The liquidator, John Whittfield, after investigating the transactions, decided that Whitfield should pursue the claim that

gives rise to the present appeal. That is, that Mr Bruce breached his duty as mortgagee to strictly account to Whitford for the proceeds of the sale of the Whitford Land under s 185 of the Act, and that Mr Hayhow and Coumat dishonestly assisted, and knowingly received the benefit of, that breach.

[17] Mr Bruce represented himself in the High Court but took no steps in this Court. Nevertheless, as we have indicated, his position, and in particular his duties, are central to the appeal, which contests Duffy J's decision that Mr Bruce breached his fiduciary duties as mortgagee.

The High Court judgment and the issues arising

[18] Duffy J's core findings were as follows:[2]

(a) Mr Bruce breached the mortgagee's duty to account for the surplus proceeds of the mortgagee sale of the Whitford Land, insofar as he accepted payments that were less than the contract price.

(b) Mr Bruce breached the mortgagee's duty to obtain the best price reasonably possible insofar as he sold the Whitford Land on terms whereby Whitford did not receive good consideration for the full sale price of the Whitford Land.

(c) Mr Hayhow and Coumat dishonestly assisted Mr Bruce in his breach of trust to account for the surplus proceeds of the sale of the Whitford Land.

(d) Coumat knowingly received and enjoyed the surplus proceeds of the sale that were held on trust for Whitford.

She also held that compound interest was available and that the parties were to file memoranda on interest.

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2 *Whitford Properties Ltd (in liq) v Bruce* [2017] NZHC 625 at [151].

[19] Mr Dalkie for the appellants raised two main points which he set out in a summary of argument:

> 1. The $1.25 million was a benefit to [Whitford]. It was paid against its debt due to the ANZ Bank, and reduced the debt by the amount of the payment.
>
> 2. The appellants have no liability as accessories since Mr Bruce was never a trustee for [Whitford] as beneficiary of any amount of money because there was no surplus.

[20] His core argument therefore related to the $1.25 million portion of the deposit under the Substitute Private Treaty Agreement. This approach limited the issues arising on appeal. In her decision Duffy J was faced with a much larger number of questions.

[21] All parties agreed that the purchase price of $10,014,956 in the Substitute Private Treaty Agreement represented the best price reasonably obtainable for the Whitford Land at the time. Thus there is no challenge to Duffy J's finding that this was the reasonable market value.[3]

[22] Mr Dalkie's criticisms of Duffy J's judgment focused on her finding that, viewed objectively, the components of the deposit that was credited to Mr Hayhow under the Substitute Private Treaty Agreement did not constitute consideration for the purchase. She held:[4]

> The problem here for the defendants is that the non-cash consideration was not good consideration vis-à-vis [Whitford]. Writing off a debt owed between Mr Bruce and Mr Hayhow is of no value to [Whitford]. Crediting Coumat with the benefit of Mr Hayhow's forfeit deposit for the tender agreement is also of no value to [Whitford]. Whilst the forfeit deposit reduced [Whitford's] debt to ANZ, the reason for the forfeiture was the failure of the purchaser under the tender agreement to settle. That transaction did not directly involve [Whitford]. Further, had there been no forfeiture, the sum payable by Mr Bruce to redeem the ANZ mortgage would have been $1.25 million more. For Mr Bruce to obtain the rights to exercise a mortgagee sale he had to pay ANZ whatever was owed under the mortgages. There is no evidence to suggest ANZ would have agreed to the assignment for a lesser payment.

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3 At [96].
4 At [95].

[23] Mr Dalkie argued that these conclusions were wrong. The crediting to Coumat of Mr Hayhow's forfeit deposit was of benefit to Whitford, because it reduced Whitford's mortgage debt. Mr Dalkie contended that ANZ could not have applied the forfeit deposit to Whitford's debt without the permission of Mr Hayhow, who had funded the deposit. Mr Hayhow only gave that permission, and the deposit was only applied to the mortgage debt, in anticipation of the Substitute Private Treaty Agreement and the sale of the Whitford Land to Mr Hayhow. It was therefore an error for the Judge to see the Substitute Private Treaty Agreement as structured in a way that deprived Whitford of the benefit of any surplus proceeds.[5] Whitford had got the benefit of the deposit by the reduction of its mortgage debt, irrespective of the fact that Whitford was not a party to the Initial Tender Agreement under which the deposit was paid.

[24] Mr Dalkie did not make detailed submissions on whether Mr Hayhow had been guilty of dishonest assistance and knowing receipt in relation to the $1.25 million. He accepted that if there had been a breach of trust by Mr Bruce, such conclusions against Mr Hayhow and Coumat were available. The thrust of his argument was that there was no breach of trust. He went further and submitted that, even if it were established that there had been a breach of the duty to account for the mortgagee sale proceeds, that was not a breach of trust of the type that could sustain a claim against Mr Hayhow for dishonest assistance or knowing receipt.

Mr Bruce's duties in relation to the mortgage

[25] The issue of the duty of a mortgagee to obtain the best price reasonably obtainable under s 176 of the Act does not arise in this case. It is agreed by both parties and indeed recorded by the Judge that the price of $10,014,956 in the Substitute Private Treaty agreement represented the best price reasonably obtainable for the Whitford Land. What is at issue in this case is the duty of the mortgagee to account for the proceeds of that sale.

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5 At [96].

[26] Section 185 of the Act provides:

> **185 Application of proceeds of sale of mortgaged property**
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> (1) The proceeds arising from the sale by a mortgagee of mortgaged property must be applied—
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> …
>
> (d) fourthly, to the payment of amounts secured by the mortgage (to the extent that those amounts have not been paid under paragraphs (a) to (c)):
>
> …
>
> (f) sixthly, to the payment of any surplus to the current mortgagor.
>
> …

The first question that arises is whether this statutory duty applies to a person in the position of Mr Bruce, where Mr Bruce has been assigned the mortgage as guarantor. Duffy J proceeded on the basis that Mr Bruce had all the duties of a mortgagee to account for the surplus proceeds arising from any sale.

[27] Section 102(1) of the Act provides:

> **102 Request to mortgagee to transfer mortgage**
>
> (1) The current mortgagor or any other person who is entitled to redeem the mortgaged property may, at any time (except a time when the mortgagee is in possession of the property), request the mortgagee to transfer the mortgage to a nominated person (except the current mortgagor).

[28] "Mortgagee" is defined in the Act as including, if the mortgage has been assigned, the assignee of the mortgage for the time being.[6] The wording is broad enough to include a s 102(1) transferee. We take the view that the obligation set out in s 185 to account to the mortgagor for any surplus applied to Mr Bruce as the mortgagee from the moment of the transfer of the mortgage to him. The language of s 185 is absolute. The mortgagee "must" apply the surplus proceeds as provided.

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6 Property Law Act 2007, s 4.

[29] Section 185 reflects the intervention of equity in relation to mortgages. The function of the mortgage went from being both security for a loan and a source of profit in lieu of interest, to being only a security for a loan and not yielding profit to the mortgagee over and above the interest permitted by law.[7] A mortgagee might not reap any benefit from the fee simple. For instance, if a mortgagee took possession, equity held it liable to account for a full rent to the mortgagor.[8] Section 185 is consistent with the general proposition in securities law that a mortgage is no more than security for the payment of a debt, reflected now in s 79 of the Act, which provides that a mortgage over land takes effect as a charge.

[30] The power of sale that is conferred on a mortgagee must be exercised only for the purpose of paying the debt, and in good faith, and not for some other purpose. This principle was given authoritative expression by the Privy Council in *Downsview Nominees Ltd v First City Corp Ltd*:[9]

> Several centuries ago equity evolved principles for the enforcement of mortgages and the protection of borrowers. The most basic principles were, first, that a mortgage is security for the repayment of a debt and, secondly, that a security for repayment of a debt is only a mortgage. From these principles flowed two rules, first, that powers conferred on a mortgagee must be exercised in good faith for the purpose of obtaining repayment and secondly that, subject to the first rule, powers conferred on a mortgagee may be exercised although the consequences may be disadvantageous to the borrower. These principles and rules apply also to a receiver and manager appointed by the mortgagee.

[31] It follows that a securityholder commits a breach of an equitable duty if it uses sale funds other than for the particular purpose of achieving payment of its debt. Once the debt has been repaid, the mortgagee must account to the mortgagor for any surplus. This principle was expressed by the English Court of Appeal in *Cuckmere Brick Co Ltd v Mutual Finance Ltd*:[10]

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7 For example, in *Cityland and Property (Holdings) Ltd v Dabrah* [1968] Ch 166, [1967] All ER 639 a mortgagee was not permitted to insert a collateral stipulation for the payment of a premium.

8 See discussion in Robert Megarry and William Wade *The Law of Real Property* (8th ed, Sweet and Maxwell, London, 2012) at [24-010].

9 *Downsview Nominees Ltd v First City Corp Ltd* [1993] 1 NZLR 513 (PC) at 522.

10 *Cuckmere Brick Co Ltd v Mutual Finance Ltd* [1971] Ch 949 (CA) at 966. See also Wayne Clark (ed) *Fisher and Lightwood's Law of Mortgage* (14th ed, LexisNexis, Wellington, 2014) at [30.46].

> Approaching the matter first of all on principle, it is to be observed that if the sale yields a surplus over the amount owed under the mortgage, the mortgagee holds the surplus in trust for the mortgagor.

[32] We note the comment of Kay J in *Charles v Jones* that while a court is reluctant to treat a mortgagee as being a trustee while money is due:[11]

> … still when he has paid himself, and has money remaining in his hands which is no longer his property, how can he be treated as other than a trustee of such money?

[33] It was held in *Chaplin v Young (No 1)* in relation to a mortgagee in possession, that:[12]

> … he stands exactly, as regards his powers, in the place of the mortgagor, and, accordingly, he is accountable to the owner of the equity of redemption for everything which he either has received or might have received, or ought to have received, while he continued in such possession.

[34] The same principle applies equally to a mortgagee who, as a consequence of a default, is selling the mortgaged property. The proceeds can only be used to discharge the debt, and beyond that the mortgagee is accountable to the mortgagor. This was summarised by Megarry and Wade in *The Law of Real Property*:[13]

> What [the mortgagee] may not do is to reap any personal advantage beyond what is due to him under the mortgage; for he is liable to account in equity for any such advantage. He is liable to account strictly, "on the footing of wilful default". This means that he must account not only for all that he receives but also for all that he ought to have received, had he managed the property with due diligence.
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> (Footnotes omitted.)

[35] Therefore a person who is exercising the powers of a mortgagee commits a breach of the equitable duty of good faith if that power is exercised otherwise than for the special purpose of enabling the assets comprised in the security to be preserved and realised for the benefit of that mortgagee.[14] The obligation to exercise the power of sale only for this purpose means that, when a mortgagee sale fails, and the

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11 *Charles v Jones* (1887) 35 Ch D 544 at 550.
12 *Chaplin v Young (No 1)* (1864) 33 Beav 330 (Ch) at 337–338.
13 Megarry and Wade, above n 8, at [25-026].
14 *Re B Johnson and Co (Builders) Ltd* [1955] Ch 634 (CA) at 661–663; and *Downsview Nominees Ltd v First City Corp Ltd*, above n 9, at 523.

mortgagee obtains funds from the forfeiture of a deposit, the duty of good faith requires those funds to be applied to reduce the mortgage debt.

Was there a breach of trust?

[36] There is little difference between Mr Black for Whitford and Mr Dalkie about the legal principles that we have outlined. The key difference was their application to the facts. Mr Dalkie submitted that the deposit of $1.25 million, which ultimately reduced Whitford's debt to ANZ, was a benefit to Whitford and was properly dealt with in the accounting for the $10,014,956 price for the Whitford Land. He submitted that it was not right to regard the deposit paid by Mr Hayhow under the Initial Tender Agreement as money that was already lost. It was wrong for the Judge to say that crediting Coumat with the benefit of the deposit was of no value to Whitford.[15] It was of value, because ANZ was not entitled to apply the forfeit deposit to the mortgage debt without Mr Hayhow's permission. Furthermore, if Whitford got the benefit of both the deposit under the Initial Tender Agreement and the deposit under the Substitute Private Treaty Agreement, it was being unjustly enriched.

The Initial Tender deposit

[37] It is necessary to consider the nature of the $1.25 million deposit paid under the Initial Tender Agreement by Mr Allen, using funds provided by Mr Hayhow and his wife. Under cl 4.2 of the Initial Tender Agreement ANZ's solicitors, Buddle Findlay, would hold the deposit as stakeholder until settlement was completed in accordance with the provisions of the Agreement. It was stated in cl 4.7: "If this contract is cancelled as a result of the Successful Tenderer's default, the deposit plus interest as provided in clause 4.9 will be forfeited to the Vendor." Clause 4.9 went on to provide that the party to whom the deposit was ultimately distributed, either on settlement or in accordance with the conditions of the tender document, would also be entitled to interest accrued thereon, if any, less withholding tax and less stakeholder's commission which would not be more than five per cent of the gross interest received.

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15 *Whitford Properties Ltd (in liq) v Bruce*, above n 2, at [95].

[38] The Buddle Findlay receipts for the deposit of 16 and 17 April 2014 showed that the deposit was paid to that firm directly by G and N Hayhow for:

> … credit of deposit funds re mortgage sale to Wayne Allen (Whitford Properties) being part deposit paid to Buddle Findlay as stakeholder on account of Wayne Ramon Allen as successful tenderer in respect of ANZ mortgagee sale tender of Whitford Properties.

[39] It is important to record what is readily apparent: the $1.25 million deposit was paid in the name of Mr Allen. Mr and Mrs Hayhow provided the funds that were used as Mr Allen's deposit, but Mr Allen was the purchaser, and it was his deposit. The sum fell under the provisions of cl 4.7 of the Initial Tender Agreement and on default was forfeited to ANZ.

[40] In fact, as we have set out, there was a default and ultimately the Initial Tender Agreement with ANZ was cancelled on 23 July 2014. The deposit was forfeit in terms of that Agreement. This was recognised by Mr Hayhow's lawyers, Barter & Co. Shortly before the cancellation in their letter to Alexander Dorrington, who acted for Mr Allen, they stated on behalf of Mr Hayhow:

> We refer to [Mr Hayhow's loan of the deposit monies to Mr Allen] simply because in the event ANZ should purport to cancel the tender contract and not return Greg Hayhow's $1.25m legal proceedings would arise.

We interpret this as meaning that if the Initial Tender Agreement was cancelled because of a failure to settle and the deposit was forfeit, Mr Hayhow would sue Mr Allen for the sum advanced. This position is consistent with later steps taken by Mr Hayhow to sue Mr Allen for the deposit.

[41] Thus at the moment of cancellation on 23 July 2014 the deposit was forfeit and could be retained by ANZ. However, ANZ could not retain it for its own benefit. It was part of the proceeds arising from the sale by a mortgagee of mortgaged property and had to be applied under s 185(1)(d) for payment of amounts owed under the mortgage. It could not be retained by ANZ for its private benefit or paid to any third party. That would be a breach of trust. It followed that at the moment of forfeiture the mortgage indebtedness was reduced by the $1.25 million deposit amount.

[42] Mr Dalkie argued that, once the Initial Tender Agreement was cancelled, ANZ could only have returned that money to the Hayhows. It could not apply the forfeit deposit to Whitford's debt. Presumably he based this submission on the fact that the Hayhows had provided the money for the deposit. However, they had paid the money in the name of Mr Allen as purchaser, as the Buddle Findlay receipts recorded. Once credited on that basis, ANZ held the deposit under the Initial Tender Agreement as stakeholder. It had sold the property to Mr Allen, and had not accepted the deposit monies on trust for the Hayhows. It had accepted it under the contractual provisions of the Initial Tender Agreement with Mr Allen. ANZ, as stakeholder while the Initial Tender Agreement was extant, had duties to Mr Allen as the other party. It owed no duties to the Hayhows.

[43] However, once Mr Allen failed to settle and the Initial Tender Agreement was cancelled, ANZ had no further contractual obligations to Mr Allen and could retain the deposit. At that point, pursuant to the equitable duties that we have outlined, ANZ was obliged to apply the deposit in the same way as it would have applied any proceeds of a sale of security; in reduction of the mortgage. This is ultimately what it did when it recorded the deposit as having been applied to the mortgage in its settlement statement of 4 August 2014.

[44] The receipt of the $1.25 million can be seen as a legitimate benefit enjoyed by Whitford and not as a gratuitous windfall. The deposit had been a pledge for the performance of the Initial Tender Agreement, and can also be seen as an aspect of the price of the option to obtain the sale.[16] Mr Allen had expressly agreed to the forfeiture upon failure to settle when he signed the Initial Tender Agreement. Whitford had, after all, lost the benefit of the sale, and Mr Allen had not honoured his pledge. The forfeiture was compensation for this failure, provided for in the contract. The forfeiture of the deposit was also of benefit to ANZ, which had the sums it was owed reduced by the deposit amount of $1.25 million. Nevertheless, if ANZ attempted again to sell to recover the still considerable outstanding balance, its duty to obtain the best price reasonably obtainable remained, namely to repay the reduced debt and pay any surplus to the mortgagor.

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[16] See the discussion concerning deposits and unjust enrichment below at [54]–[56].

[45] In our view s 185 obliged ANZ to account to Whitford for the forfeit deposit, irrespective of the fact that the deposit was funded by the Hayhows. Section 185 is directed to the proceeds "arising from the sale by a mortgagee of mortgage property". There was for a period a sale to Mr Allen under the Initial Tender Agreement, and the deposit was proceeds from that sale. It does not matter that this sale did not proceed to settlement. Further, as we have outlined, a concurrent duty to apply the purchase price in reduction of the debt arose in equity in relation to the proceeds, and the duty was not limited only to sales that proceeded to a settlement. It applied also to sales that did not proceed, but from which funds became available to the mortgagee.[17]

Steps taken by Mr Hayhow

[46] Following the cancellation of the Initial Tender Agreement Mr and Mrs Hayhow undoubtedly had a right of action against Mr Allen for the $1.25 million they had provided to him for the deposit. Indeed, Mr Hayhow formally sought to join Mr Allen to this proceeding as an additional party. The application was contested, and was determined by Associate Judge Doogue who refused to join Mr Allen.[18] The Judge recorded:

> [15] By his third party claim, Mr Hayhow appears to be alleging that he paid the $1.25 million to the bank which forfeited that amount when the joint venture did not proceed as a result of the failure of Mr Allen to obtain the necessary finance. He further apparently claims that if he is required to account for the proceeds of sale as a mortgagee, he will be required to pay the $1.25 million a second time, in effect. The $1.25 million is over and above the figure which was owing to and paid to the bank. Therefore, ANZ, as the initial mortgagee, obtained an advantage to that extent. Mr Hayhow and the other assignees of the mortgage from the bank, similarly, must account to the mortgagor for any money received under the mortgage which exceeds the amount the mortgagor owed to the bank, it is alleged. Mr Hayhow wants to recover that sum from the proposed third party.

[47] It can be seen that, at that stage, Mr Hayhow was taking at least an alternative position that the deposit was forfeit. He sought compensation for the deposit amount from Mr Allen on the basis of Mr Allen's failure to settle the sale under the Initial Tender Agreement. Further, on 31 July 2014 Mr Hayhow had signed an instruction confirming that he did not dispute or challenge the forfeiture of the deposit to ANZ:

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17 As best as we can understand the respondent's notice to support the judgment on other grounds, this conclusion encompasses that other ground.

18 *Whitford Properties Ltd (in liq) v Bruce* [2016] NZHC 58.

> … pursuant to the cancellation of the sale and purchase agreement or the application of such funds by ANZ Bank New Zealand Ltd in reduction of the indebtedness of the mortgagor, Whitford Properties Ltd, to ANZ Bank New Zealand Limited.

[48] However, after the collapse of the Initial Tender Agreement Mr Hayhow was plainly of the mistaken view that he should be able to recover the lost deposit not from Mr Allen directly but by treating it as a credit to the fair market price of the Whitford Land. He deposed:

> Despite the Substitute Private Treaty Agreement stating that the gross sale price included the 'deposit' of $2,560,054 comprised of the $1,310,054 being owed by Mr Bruce to me and the forfeited deposit of $1,250,000, there was never any intention by Coumat or myself to make cash payment of the Disputed Funds under the agreement to purchase the property. The amendments were a notional record only as Mr Bruce required that the debt be forgiven, and the document was intended to recognise that, the $1,250,000 having been paid and applied already in reduction of [Whitford's] mortgage debt.

[49] The attitude of Mr Hayhow and Mr Bruce to the arrangement is encapsulated in this statement by Mr Hayhow:

> It was never my intention to pay more than the ANZ mortgage debt which was reduced by my $1,250,000 tender deposit paid to them. The amendments made to our Private Treaty Agreement and reflected in the Substitute Private Treaty Agreement were simply a record of Mr Bruce and my arrangement in respect of the debt he owed me and the Deposit that I had paid. I had no discussion with Mr Bruce as to any expectation that I pay more for the Whitford Property than the ANZ mortgage debt. I would have refused to do so as it is an absolute nonsense for me to pay an additional $2,560,054 (being his debt of $1,310,054 and the deposit of $1,250,000) to Mr Bruce to then pay to [Whitford] when they were in fact amounts due to me. Nor do I think for a moment that Mr Bruce has any expectation that a further cash sum would be paid.

[50] These statements show Mr Hayhow's lack of understanding that the deposit had already been lost by Mr Allen, and could only be recovered by action against him. Mr Dalkie argued in response that as matters unfolded there was in fact no sale in respect of the Initial Tender Agreement for which the $1.25 million was paid. The Agreement was cancelled and ANZ could not retain the money. It had to be returned to Mr Hayhow. He sought to rely on Mr Hayhow's instruction to ANZ on 31 July 2014 stating in respect of the $1.25 million deposit:

1. we assert no claim to such funds (or any interest in relation to those funds): and

2. we do not dispute and will not challenge the forfeiture of such funds to ANZ Bank New Zealand Limited pursuant to the cancellation of the sale and purchase agreement or the application of such funds by ANZ Bank New Zealand Limited in reduction of the indebtedness of the mortgagor, Whitford Properties Limited, to ANZ Bank New Zealand Limited.

[51] Mr Dalkie submitted that, by seeking Mr Hayhow's permission to apply the forfeit deposit to the mortgage debt, ANZ acknowledged that it was not entitled to do so without that permission. In fact, Mr Hayhow had no basis on which to unwind the forfeiture. It had already happened and lawfully so, in accordance with the unchallenged provisions of the Initial Tender Agreement. The monies had been forfeit from the moment of cancellation on 23 July 2014. Mr Hayhow could not retrospectively instruct ANZ to return the deposit and deprive Whitford of the benefit of the reduction of its indebtedness. As it turned out, the forfeiture was a benefit for Whitford, but one to which it was fully entitled by virtue of the cancellation of the Initial Tender Agreement.

[52] Thus the $1.25 million could not be treated by Mr Bruce and Mr Hayhow as forming part of the consideration provided in relation to the purchase price for the Whitford Land under the Substitute Private Treaty Agreement. It could not be so treated because it was already a credit against the mortgage, to the benefit of Whitford. As a further point, if the logic of Mr Dalkie's argument was correct, then it was not Coumat that could claim the credit, as it did under the Substitute Private Treaty Agreement. If the deposit was not forfeit, it would have been refundable to the Hayhows who had paid it on behalf of Mr Allen, and not Coumat, which had no involvement whatsoever in the Initial Tender Agreement.

The $1,310,054

[53] These principles apply equally to the credit of $1,310,054 that Coumat received under the Substitute Private Treaty Agreement in exchange for Mr Hayhow forgiving Mr Bruce's unsecured personal debt. Indeed, Coumat did not seek to argue otherwise in respect of that sum. Mr Bruce was essentially obtaining a personal benefit for himself in having the debt of $1,310,054 repaid, effectively at the cost of Whitford,

which was deprived of that amount. Mr Hayhow was also indirectly getting a benefit, in that his company Coumat was receiving a credit for the unsecured and perhaps otherwise irrecoverable money that he and Mrs Hayhow were owed by Mr Bruce (including a huge interest component).

Unjust enrichment

[54] Mr Dalkie argued that there was a claim of unjust enrichment available to the Hayhows. If the $1.25 million was treated the way it had been treated by Duffy J in her judgment, Whitford had benefited by receiving monies to which it had no claim at the time they were received. He relied on the following statement from *Goff & Jones: The Law of Unjust Enrichment*:[19]

> Since contractual provisions governing payment for a benefit will implicitly displace a claim for unjust enrichment in respect of that benefit, careful analysis may be needed in order to ascertain whether the benefit in question falls within the contract.

[55] Unjust enrichment was not pleaded as a set-off or counterclaim in the High Court, and Mr Black objected to it being raised on appeal. We deal with it briefly, as there is no merit in this argument. Plainly the time honoured contractual provision enabling the forfeiture of a 10 per cent deposit does not give rise to a claim for unjust enrichment, as the learned authors of *Goff & Jones* recognise in the above quote. The function of deposits was stated by Fry LJ in *Howe v Smith*:[20]

> [A deposit is] an earnest to bind the bargain so entered into, and creates by the fear of its forfeiture a motive in the payer to perform the rest of the contract.

[56] There is nothing unjust in parties agreeing, as part of a commercial contract, to a set sum as the penalty for a failure to settle. The deposit can be seen as a pledge for the performance of the contract.[21] Its primary purpose is to guarantee that the purchase will go ahead.[22] It is also an aspect of the price of the opportunity to obtain the sale.[23]

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19 Charles Mitchell and others (eds) *Goff & Jones*: *The Law of Unjust Enrichment* (9th ed, Sweet and Maxwell, London, 2015) at [3–35].

20 *Howe v Smith* (1881) 27 Ch D 89 at 101.

21 *Garratt v Ikeda* [2002] 1 NZLR 577 (CA) at [34].

22 *Soper v Arnold* (1889) 14 App Cas 429 (HL) at 435, quoted in *Garratt v Ikeda*, above n 21, at [35].

23 See Peter Watts "Forfeiture of Deposits: Enforcing Agreements" [2002] NZ L Rev 19 at 24. It is not necessary for us to consider the academic debate on the correctness of *Garratt v Ikeda*: see D W McLauchlan "Forfeiture of Deposits: Punishing the Contract Breaker" [2002] NZ Law Review 1; D W McLauchlan "Forfeiture of Deposits: A Reply" [2002] NZ Law Review 33;

When a purchaser defaults there is nothing unjust in it having to meet this contractual pledge, to which it has expressly agreed. Mr Allen must be taken as having known and intended that if he defaulted the deposit would be forfeit. The amount of 10 per cent is the standard for such contracts.[24] Insofar as the vendor, or in this case the mortgagor, obtains a benefit, it is a contractual benefit to which it is directly entitled in the case of the vendor, and indirectly entitled in the case of the mortgagor. There is no injustice.

Conclusion on Mr Bruce's duties

[57] It follows that we agree with the decision of Duffy J that Mr Bruce breached the mortgagee's duty to account for the surplus proceeds from the mortgagee sale, so far as he accepted a credit of a total of $2,560,054 as the deposit under the Substitute Private Treaty Agreement, which he did not make available to Whitford. To the contrary, in respect of the $1.25 million, Coumat got a $1.25 million credit it had not earned or paid for. The deposit paid by Mr Allen under the Initial Tender Agreement was contractually forfeit, and it could not be appropriated by Mr Bruce and Coumat in a later sale.

[58] In respect of the $1,310,054, Mr Bruce and Mr Hayhow received the benefit of the money: Mr Bruce's personal debt was forgiven and Mr Hayhow (through Coumat) obtained repayment of the unsecured and doubtful debt owed by Mr Bruce. Together, the credit for these amounts reduced the price that should have been paid for the Whitford Land. Mr Bruce breached his s 185 and equitable duties in treating the $2,560,054 as already paid (and therefore a credit available to Coumat), rather than requiring payment of the full sale price.

Liability of Mr Hayhow and Coumat for knowing receipt or dishonest assistance

[59] It is not necessary to consider this issue in detail, as Mr Dalkie accepted that, if Mr Bruce was in breach of trust, Mr Hayhow was liable for dishonest assistance.

Brian Coote "Unpaid Deposits and the Contractual Remedies Act 1979" (2002) 8 NZBLQ 142; and Andrew Geddis "Garratt v Ikeda" (2002) 18 JCL 250.

24 *Garratt v Ikeda*, above n 21, at [40].

[60] For a stranger to be personally liable under the doctrine of knowing receipt or dishonest assistance there must have been a breach of trust or other fiduciary obligation.[25] As Smellie J outlined in *Equiticorp Industries Group Ltd v The Crown*, there are three necessary elements for a claim of knowing receipt and accessory liability.[26] First, the plaintiffs must show a disposal of funds by a person owing a fiduciary duty to them in breach of that fiduciary duty or on some other unauthorised basis. Second, the defendant must receive the benefit of those funds. Third, there must be knowledge by the defendant that the payment was in breach of the fiduciary duty or other unauthorised act. That knowledge is assessed objectively, and is not dependent on subjective dishonesty.

[61] Plainly all three elements exist here in relation to Coumat. First, Mr Bruce agreed to a payment structure for the Whitford Land whereby the $2,560,054 deposit was not paid and not available to Whitford, in breach of trust. Second, Coumat received the benefit of that breach of trust in the form of a reduced purchase price for the Whitford Land. While no monies were received by Coumat, Coumat got monies' worth in that it was given a credit on a purchase where the sale price was at market value. Coumat had contrived a situation where it purchased at an under-value at Whitford's expense. Third, Coumat, through its director Mr Hayhow, knew that the credit involved appropriating the deposit for itself, and it was for monies that would otherwise go to paying off the mortgage, with the surplus going to Whitford.

[62] In relation to Mr Hayhow, he did not directly receive the benefit, but he is liable for knowing assistance. As was stated by Lord Nicholls in *Royal Brunei Airlines v Tan*:[27]

> Stated in the simplest terms, a trust is a relationship which exists when one person holds property on behalf of another. If, for his own purposes, a third party deliberately interferes in that relationship by assisting the trustee in depriving the beneficiary of the property held for him by the trustee, the beneficiary should be able to look for recompense to the third party as well as the trustee.

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25 *Selangor United Rubber Estates Ltd v Cradock (No 3)* [1968] 1 WLR 1555 (Ch) at 1579; *Westpac Banking Corp v Savin* [1985] 2 NZLR 41 (CA) at 52; and *Equiticorp Industries Group Ltd v The Crown* [1998] 2 NZLR 481 (HC) at 540.

26 *Equiticorp Industries Group Ltd v The Crown*, above n 25, at 540.

27 *Royal Brunei Airlines v Tan* [1995] 2 AC 378 (PC) at 386.

[63] As we have set out, Mr Hayhow knew of the facts constituting the breach of fiduciary duty. He knew of the credit to his company, Coumat. He was its director and sole shareholder. In negotiating the arrangement and implementing it for Coumat at the expense of Whitford, he was, objectively assessed, dishonest. It was plain that in obtaining payment of Mr Bruce's debt to him personally (the bulk of which was interest at 400 per cent) he was getting a credit at the expense of Whitford, which it would have otherwise received as funds. While he may not have understood the law relating to deposits, looking at the matter objectively he should have known that Whitford already had the benefit of the forfeit deposit on the Initial Tender and he could not escape his obligation to pay the $1.25 million by offsetting his loss.

[64] It follows that we agree with Duffy J's conclusions that Mr Bruce had breached trust, that Coumat knowingly received and enjoyed the surplus proceeds of the sale, and that Mr Hayhow dishonestly assisted Mr Bruce in his breach of trust.[28] Whitford has proven this aspect of its claim.[29]

Conclusion

[65] We uphold the Judge's decision.

[66] We decline the application to adduce new evidence. The proposed new evidence was to the effect that the Whitford Land had been on-sold by Coumat in late 2016 for a price in the vicinity of $22 million or more, a great profit. However, given that it is agreed that when the Whitford Land was sold the best price reasonably obtainable was the $10,014,956 sale price, evidence of later sales is irrelevant.

Result

[67] The application for leave to adduce further evidence is declined.

[68] The appeal is dismissed.

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28 *Whitford Properties Ltd (in liq) v Bruce*, above n 2, at [112] and [116].

29 Given our conclusion there is no need for us to deal specifically with a notice of the respondent to support the decision appealed from on another ground. As best we can understand the notice, our decision does, in any event, uphold the decision on that new ground. See above n 17.

[69] The parties accept that costs must follow the event. The appellants must pay the respondent costs for a standard appeal on a band A basis and usual disbursements.

Solicitors:
Inder Lynch, Papakura for Appellants
Alexander Dorrington Lawyers, Auckland for Respondent