IN THE SUPREME COURT OF NEW ZEALAND

SC 46/2011
[2012] NZSC 72

BETWEEN	NEIL TONY HICKMAN AND ORS First Appellant
AND	DAVID JOHN LESTER AND ORS Second Appellant
AND	ANTHONY COLLINGWOOD AND ORS Third Appellant
AND	NORMAN AND MARIE HERRICK Fourth Appellant
AND	TURNER AND WAVERLEY LIMITED (FORMERLY TURN AND WAVE LIMITED) First Respondent
AND	GREENSTONE BARCLAY TRUSTEES LIMITED Second Respondent
AND	GRAFTON PROJECTS LIMITED (FORMERLY ICON CENTRAL LIMITED) Third Respondent

Hearing:	7 - 9 November 2011
Court:	Elias CJ, Tipping, McGrath, William Young and Anderson JJ
Counsel:	P J Dale, N R Campbell and D W Grove for Appellants S H Barter for Appellant Herrick D J Chisholm and G P Blanchard for First Respondent D J Neutze for Second Respondent B O'Callahan for Third Respondent
Judgment:	9 August 2012

JUDGMENT OF THE COURT

A **The appeals are allowed.**

B **The SPAs executed at the same time as, or after, the corresponding Blue Chip investment product agreements were entered into are declared to be unenforceable under s 37 of the Securities Act 1978.**

C **The High Court is to determine whether SPAs, entered into before the corresponding Blue Chip investment products were executed, were subscriptions for securities.**

D **The cases are otherwise generally remitted to the High Court to make such further orders as may be consistent with this judgment.**

E **The respondents are to pay the appellants costs $75,000 and usual disbursements.**

F **Costs in the High Court and Court of Appeal are to be as determined by those courts.**

REASONS

Para No

ELIAS CJ, McGRATH, WILLIAM YOUNG AND ANDERSON JJ

(Given by William Young J)

Table of Contents

Introduction

[1] The appellants participated in investment schemes marketed by the Blue Chip group of companies.[1] These required them to commit to the purchase of apartments in one or more of three proposed developments on land which had originated with entities associated with Blue Chip but which, in two cases, had by then been sold to independent third party developers. The appellants relied very heavily on the Blue Chip parties honouring their financial promises, which, in the event, they did not do. If the appellants are held to the purchase agreements with the developers, they will suffer very substantial losses.

[2] The appellants maintain that when Blue Chip marketed its investment schemes, it was offering securities to the public within the meaning of the Securities Act 1978 and that it did so without meeting the associated requirements. On this basis they seek to impeach the closely associated agreements for sale and purchase (SPAs) they entered into with the developers. These arguments (and a number of

[1] What we mean by this is discussed below at [4].

other arguments which are no longer pursued) have been dismissed by Venning J in the High Court[2] and by the Court of Appeal.[3]

[3] As will become apparent – and in respectful disagreement with Venning J and the Court of Appeal – we have come to the conclusion that the appellants' Securities Act arguments are correct. When Blue Chip was marketing its investment schemes, it acted in breach of the Securities Act and thus brought into play s 37 of that Act which renders unenforceable the allotment of improperly marketed securities and the associated subscription for such securities. We also conclude that the unenforceability prescribed by s 37 extends to the SPAs; this primarily because the way the investors subscribed for the securities marketed by Blue Chip was by entering into the SPAs. In the result, we hold that the SPAs are unenforceable under s 37(4).[4] As well, we consider that the developers are also issuers, giving rise to entitlements to relief under s 37(5).

The facts

Blue Chip and its business model

[4] Blue Chip (New Zealand) Ltd[5] was established in 2000 as a promoter of property investments. Mr Mark Bryers was its driving force. Unless there is need for greater particularity, we will refer to this company, its subsidiaries and associates along with companies perhaps more closely linked to Mr Bryers, as "Blue Chip".

[5] Blue Chip marketed four investment products:

- the mainstream agreement;
- the joint venture agreement (JVA);

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2 *Lester v Greenstone Barclay Trustees Ltd* [2010] 3 NZLR 67 (HC) [Greenstone]; *Hickman v Turn & Wave Ltd* HC Auckland CIV-2008-404-5871, 25 November 2009 [TWL]; *Icon Central Ltd v Collingwood* HC Auckland CIV-2008-404-7424, 25 November 2009 [Icon].

3 *Hickman v Turn and Wave Ltd* [2011] NZCA 100, [2011] 3 NZLR 318.

4 This conclusion applies only to those SPAs which were entered into at the same time as the relevant investor committed to the corresponding Blue Chip product. There is at least one, and may be more, instances where the SPA was entered into earlier, see below at [108].

5 This was the name of the company at all times material to this litigation. It later changed its name to Blue Chip Financial Solutions Ltd and then Northern Crest Investments Ltd, its current name.

- the premium income product (PIP); and
- the put and call agreement (PAC).

[6] Under the mainstream agreement, the investors purchased apartments which were subject to leases with the rent guaranteed by Blue Chip. There were associated agreements for the sale and purchase of a furniture pack and for property management. None of the appellants in this case acquired the mainstream product although it was envisaged that the apartments the appellants purchased would later be sold again, with the new purchasers entering into mainstream agreements.

[7] The other three products (which we will discuss in a little more detail shortly) were all associated with a Blue Chip strategy which was based around:

(a) Blue Chip identifying and securing sites suitable for apartment buildings;

(b) either selling such sites to an independent developer who would build an apartment building on the site, or alternatively Blue Chip itself directly putting in train the planning and funding arrangements for the erection of such a building;

(c) Blue Chip selling apartments "off the plan" to short-term investors and in this way generating sufficient pre-sales to allow funding to be drawn down for the construction of the apartment buildings and at the same time generating underwriting fees for Blue Chip based on the selling prices of the apartments; and

(d) Blue Chip, in due course, locating a second purchaser for each apartment whose purchase payment would enable the original investor to be taken out.

[8] Whether Blue Chip made profits on the initial securing of the development sites and their on-sale to developers was not explored before us and is not material to the outcome of the appeals. But there were plainly other benefits. The arrangements facilitated the receipt by Blue Chip of underwrite fees which were essentially

commissions on the sales made to the investors. More generally, according to material generated by Blue Chip, these arrangements enabled it to maintain control over a significant number of apartments which were, in effect, "on the shelf" and could later be sold to investors under the mainstream agreement (who were said to prefer "immediate settlement stock"). Any capital gain derived on such further sales would accrue, either entirely or substantially, to Blue Chip.

[9] The returns for the investors were in the form of "fees" which, in the case of the JVA product and particularly the PIP, were functionally very similar to interest and in the case of the PAC product involved a sharing of Blue Chip's underwrite fee. Assuming that all went according to plan, that was, for the investors, either it, or just about it.[6] In return, they became unconditionally committed to the purchase of the apartments and they paid the required deposits.[7] The investors' outgoings were either covered by the fees payable by Blue Chip or were the subject of indemnities.[8]

The details of the investment products involved in the case

[10] The JVA was the form of investment in issue in *GE Custodians v Bartle*.[9] The investor agreed to purchase an apartment and furniture pack but also agreed, jointly with Blue Chip, to establish a joint venture entity to engage in the business of owning and leasing the apartment. The investor was required to fund the purchase of the apartment and the associated furniture pack. The return for the investor was a procurement fee (in the nature of interest). Blue Chip was to meet all outgoings on the borrowing and property. The joint venture was intended to last for approximately four years at which point it was envisaged that the property would be sold with 95 per cent of any capital gain going to Blue Chip and the balance (five per cent) accruing to the investor.

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6 In the case of the JVA product, the investor would also receive five per cent of any capital gain.
7 In some instances this was effected by the provision of bonds.
8 We are not using the word "indemnities" in a technical sense because there were a number of contractual mechanisms which were intended to ensure that investors would be protected from the practical (although not necessarily the legal) requirement to make payments other than those specifically contemplated and that, one way or another, they would eventually be reimbursed in relation to such payments as they did make.
9 *GE Custodians v Bartle* [2010] NZSC 146, [2011] 2 NZLR 31, although there may have been some differences between the JVA in issue in that case and the JVAs which are the subject of the present appeals.

[11] The risks for the investor were associated with the following features of the transactions:

(a) the prices at which the joint ventures acquired the apartments included substantial underwrite fees, in the nature of commissions, paid to Blue Chip;

(b) the amount borrowed by the investor included not only the price of the apartment (including the commission) but also the furniture pack and a working capital payment (which provided a fund from which the procurement fees could be paid);

(c) the income generated by the apartments did not cover borrowing costs;

(d) as a result of factors (a), (b) and (c), the success or failure of the investment was dependent on either continuing substantial growth in apartment values or the substance of Blue Chip's promises; and

(e) because many of the investors had little or no independent income and had mortgaged their existing homes to raise the money required to participate in the scheme, the failure of the investment meant that they might well lose their homes.

[12] Under the PIP, the investor agreed to purchase an apartment and furniture pack and was required to pay a ten per cent deposit which was held in the trust account of the property developer's solicitors with interest accruing for the benefit of the investor or Blue Chip depending on who eventually settled the purchase. The sequence of events was that the PIP agreement was entered into conditionally upon: (a) execution by the investor of the SPA and a deed on nomination, (b) Blue Chip securing execution by the developer of those documents within 10 days and (c) approval of the PIP agreement by an authorised officer of Blue Chip within the same period of 10 days. Counsel for the developers submitted that this meant that it was possible for the investor to become bound under the SPA without Blue Chip committing to the PIP under the third of the conditions. We do not see this as plausible either (a) legally, because we think that Blue Chip could not properly have

put the SPA to the developer without at the same time committing to the PIP or (b) commercially, because it is inconceivable that it would do so.

[13] From payment of the deposit until settlement, Blue Chip paid the investor a monthly option fee amounting to a return on the deposit of approximately 16 per cent per annum. These fees were linked to Blue Chip having an option to acquire the apartment from the investor prior to settlement. If Blue Chip exercised this option, the investor received back the deposit but not the interest. If Blue Chip did not exercise the option, the investor was required to complete the purchase of the apartment with Blue Chip (a) agreeing to pay the investor's reasonable costs of settlement including the costs of borrowing the balance required to settle and (b) retaining an option to acquire the apartment at the original purchase price.

[14] The risks to the investor were similar to those identified above at [11] save that the investor was not making a working capital contribution and thus the underlying property value growth assumptions were not as heroic as in the case of the JVA.

[15] Under the PAC agreements, the investor was required to enter into agreements to acquire an apartment and furniture pack and to pay the required deposit (or enter into an approved bond). There were put and call options under which Blue Chip could call for, or have put to it by the investor, the right to acquire the apartment or the apartment itself (if settlement had by then occurred). Blue Chip was to pay a call option fee which was typically $7,500 and was payable within 14 days of Blue Chip receiving an underwrite fee from the developer. It follows that the PAC agreement disclosed to the investor that Blue Chip would be receiving an underwrite fee from the developer. Many of the PAC investors were either associated with Blue Chip or had family associations with someone who was.

[16] The risks for the investor were similar to those associated with the PIP.

The Barclay development

[17] The Barclay was developed by Greenstone Barclay Trustees Ltd.[10] Its directors are Messrs John Abel-Pattinson and Kevin Cox. They were approached by Mr Bryers in October 2005 about a property in Albert Street, Auckland, which was subject to an option in favour of Blue Chip. He also told them that Blue Chip had a pool of investors available to purchase apartments. It was agreed that Greenstone would buy the site and would build an apartment building on it. Blue Chip was to introduce its investors as purchasers for the apartments. Profit share and underwrite agreements were completed between the parties on 24 March 2006 (although the profit share agreement was not engaged given the events that happened).

[18] The development was financed primarily by Westpac Bank. The Westpac facility was subject to a number of conditions which had to be satisfied before funds would be released - most significantly, pre-sales of apartments on an arm's length basis to the value of $39 million pursuant to SPAs in a form to be supplied to Westpac and not varied. The substance of the underwrite agreement was that if Greenstone had not sold all the apartments by a specified date, Blue Chip as underwriter was to purchase, to the maximum of the underwritten amount of $20 million, any apartments remaining unsold. In exchange for providing the underwriting, Blue Chip was to be paid a fee of 12.6 per cent of the sale price of each unit sold. Although the underwrite agreement provided for the use of real estate agents, in practice all sales were made through Blue Chip's licensees and sales agents. Greenstone began to receive SPAs from April 2006 and SPAs had been entered into for most of the apartments by October 2006.

[19] Under the SPAs, the deposits were usually 15 per cent of the purchase price with the balance payable on the settlement date. The properties were sold subject to lease.

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10 Now called 74 Albert St Ltd.

The Bianco

[20] Turn and Wave Ltd (TWL),[11] the sole director of which was, and remains, Mr Tim Manning, acquired a site on the corner of Turner and Waverley Streets from Blue Chip with a view to developing an apartment building to be called the Bianco. Under associated underwriting arrangements, Blue Chip was to underwrite sales in return for underwrite fees of either 12.6 or 15 per cent of the purchase price of the units depending on whether the unit was to be serviced. Westpac was again the primary funder. Westpac's special funding conditions were much the same as those specified for the Greenstone development.

[21] The sales and marketing of units in the Bianco development began about October 2006. At first, sales were slow but began to increase in December 2006. From mid-January to March 2007, sales were achieved at a very high rate. Many of them were achieved by Blue Chip using the PIP.

[22] The SPAs entered into by TWL as vendor and the investor were broadly similar to those used in relation to the Barclay development.

Icon

[23] Icon Central Ltd[12] owned a property at St Martins Lane, Auckland. From the date of its incorporation on 14 February 2007 until 30 October 2007, Mr Bryers was its only shareholder and director. On 30 October 2007 the shares in Icon were transferred to Paxton Pacific Group Ltd, a company owned by Messrs Mudgway and Ross. On the same date, Mr Bryers resigned as director of Icon and Messrs Mudgway and Ross were appointed in his place. By this stage, substantial progress had been achieved in putting together the planning and funding for an apartment building on the St Martins Lane property. Also, sufficient pre-sales had been attained to enable development funds to be drawn down from Westpac pursuant to funding arrangements which were similar to those in respect of the Barclay and Bianco developments.

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11 Now called Turner and Waverley Ltd.
12 Now called Grafton Projects Ltd.

[24] These pre-sales were generated pursuant to an underwrite agreement between Icon and BFB Underwriters Ltd (BFB). BFB was controlled by Messrs Bell and Flowerday who held senior positions in the Blue Chip organisation. BFB was a wholly-owned subsidiary of Mide Ltd. Mide was incorporated on 31 August 2007 to operate the New Zealand business of Blue Chip. Initially, Mr Bell was the sole director of Mide but Mr Flowerday was appointed an additional director on 4 October 2007. The underwrite agreement required BFB as underwriter to agree to underwrite the sale of the units up to the maximum of the underwrite amount (around $73 million) and in return BFB was to receive an underwrite fee of 15 per cent of the sale price of each unit sold. The underwriting agreement was, in some respects, dissimilar to those entered into in relation to the Barclay and Bianco developments, but the differences are not material to the resolution of the present appeals. In the balance of this judgment, references to Blue Chip can be taken to encompass, where relevant, BFB.

[25] The SPAs were similar to those entered into in respect of the other developments save that these were all signed by Mr Bryers on behalf of the vendor.

Blue Chip's marketing methods

[26] Blue Chip's marketing of the Barclay and Bianco developments was through its sales force. Most investors were introduced to the apartments in these developments and, at the same time to the JVA and PIP arrangements, through Blue Chip's marketing strategy which included cold calling by telephone and public presentations. Usually, investors were existing clients of the sales agents or were referred to them by others.

[27] The sales agents assisted investors in the arranging of finance for the purchase of the apartments. They, in turn, would authorise Blue Chip to seek finance on their behalf. The process usually culminated in the investor signing the SPA for the relevant apartment and the documentation for the Blue Chip products.

[28] The Icon development was marketed using both the PIP and PAC products. The marketing of Icon apartments associated with sales achieved using the PIP was

essentially the same as that just described. The sales achieved using the PAC product, however, were primarily to people who were associated with Blue Chip and its sales force.

Were the JVA, PIP and PAC products securities for the purposes of the Securities Act?

A preliminary comment

[29] Fundamental to the arguments of the appellants is the contention that Blue Chip's marketing of its JVA, PIP and PAC products amounted to the making of offers to the public of securities. The lawfulness of such offers is subject to compliance with the requirements of:

(a) s 33(1) (as to, most relevantly, prospectuses); and

(b) in the case of debt securities, s 33(2) (relating to the appointment of a trustee).

It is common ground that Blue Chip did offer its products to the public. It is also common ground that if s 33(1) and (2) were engaged, their requirements were not satisfied. It follows that if the products were securities within the meaning of the Securities Act and Blue Chip's conduct was not exempted from the operation of the Act, it was in breach of the Securities Act – doubly so if the products were debt securities.

[30] In this section of the judgment we address the question whether Blue Chip's products were securities as defined in the Securities Act. In the course of doing so, we examine the general structure of the Act, including its provision of various exemptions and the application of one of those exemptions to the products sold by Blue Chip.

[31] The appellants maintain that all products were debt securities. They also contend that the JVA product was also an equity security. For reasons which will

become apparent, we consider that the primary issue in relation to this aspect of the case is whether the products were debt securities and we propose to focus on this issue accordingly. We will, however, address in passing the equity security argument at the end of this section of the judgment.

Relevant provisions and definitions as to the debt securities argument

[32] Section 37 relevantly provides:

> **Void irregular allotments**
>
> (1) No allotment of a security offered to the public for subscription shall be made unless at the time of the subscription for the security there was a registered prospectus relating to the security.

As well, under s 33(1) no offer of securities may be made by or on behalf of an issuer to the public for subscription unless made in, or accompanied by, an authorised advertisement, investment statement or registered prospectus. And s 33(2) requires the appointment of a trustee where debt securities are offered to the public.

[33] The text of ss 37(1) and 33(1) requires focus on a number of terms which are all defined in the Act. These terms are:

(a) security;

(b) debt security;

(c) issuer;

(d) subscribe;

(e) offer; and

(f) allot.

[34] "Security" is defined in s 2D of the Act in this way:

2D Meaning of security

(1) In this Act, unless the context otherwise requires, the term **security** means any interest or right to participate in any capital, assets, earnings, royalties, or other property of any person; and includes—

(a) an equity security; and

(b) a debt security; and

...

(f) any interest or right that is declared by regulations to be a security for the purposes of this Act;

...

but does not include any such interest or right (other than a security referred to in paragraph (f)) that is declared by regulations not to be a security for the purposes of this Act.

[35] "Debt security" is defined in s 2 as meaning:

> any interest in or right to be paid money that is, or is to be, deposited with, lent to, or otherwise owing by, any person ...

[36] The other relevant definitions in s 2 are as follows:

(a) "Issuer", as meaning:

> (a) in relation to an equity security or a debt security, ... the person on whose behalf any money paid in consideration of the allotment of the security is received:

(b) "Subscribe", as including:

> purchase and contribute to, whether by way of cash or otherwise; ... .

(c) "Offer", as including:

> an invitation, and any proposal or invitation to make an offer; ... .

(d) "Allot", as including:

> sell, issue, assign, and convey; … .

Given the definition of “issuer”, it is necessary finally to note that “money” is defined as including “money’s worth”.

The competing approaches of the parties

[37] According to the appellants, the definition of “debt security” encompasses each of the three Blue Chip products because they conferred on the investors the right to be paid money that was to be owing to them by Blue Chip. Although that money could not be said to have been deposited with, or lent to anyone, it was nonetheless “otherwise owing”.

[38] The primary argument for the developers is that in the definition of “debt security” the words “otherwise owing” should be read ejusdem generis with “deposited with” and “lent to” and thus include only indebtedness which is of the same general nature as an obligation to repay money that has been “deposited with” or “lent to” whoever has the payment obligation. Associated with this argument was the broader contention that, at the very least, the concept of money which “is otherwise owing” is confined to obligations to repay to a subscriber money previously paid by the subscriber to the issuer. The Court of Appeal accepted the developers’ primary argument.[13]

[39] The developers also maintained that in relation to the PIP and PAC products, Blue Chip was not an “issuer” because the money which was paid (being the deposits) went to the developers with the result that Blue Chip was not the “person on whose behalf any money paid in consideration of the allotment of the security is received”. The developers succeeded on this point before Venning J.[14]

[40] The analysis which these arguments require is best preceded by discussion of the relevant legislative history, the general structure of the Securities Act and the leading decisions on the scope of the “debt security” definition.

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[13] See *Hickman*, above n 3, at [306]–[316].
[14] See *Greenstone*, above n 2, at [280]; *TWL*, above n 2, at [287]–[291] and *Icon*, above n 2, at [224]–[225] and [239].

The relevant legislative history

[41] Prior to the enactment of the Securities Act, only piecemeal legislative requirements applied to the soliciting of investment money from the public. These requirements were found in the Companies Act 1955 (ss 47–60 of which initially addressed offers by companies to the public of shares and debentures), the Protection of Depositors Act 1968 (requiring the appointment of a trustee when deposits were solicited from the public by a natural person) and the Syndicates Act 1973 (imposing restrictions on the marketing of investments in syndicates[15]).

[42] Section 48 of the Companies Act 1955 prohibited, in an awkwardly roundabout way, the issuing, to the public and without a prospectus, of "any form of application for shares in or debentures of a company". This was supplemented by s 48A (as inserted in 1960) which deemed those provisions to apply to any invitation to the public "to deposit money with or to lend money to any company". These provisions only applied to the raising of money by companies, thus leaving a loophole later filled by the Protection of Depositors Act 1968 which addressed advertisements inviting the public to "deposit money with" any natural person.[16] Under this Act, "deposit" was defined in s 2 as being a loan.

[43] When introducing the Securities Advertising Bill 1977 (later enacted as the Securities Act 1978), the Minister of Justice commented:[17]

> The purpose of the Bill ... is to consolidate and amend the law relating to the raising of investment money from the public. The Bill follows a series of financial collapses in recent years, which have drawn attention to the need for legislation to give a greater degree of protection to the public. Commercial entities have been offering to the public an increasing variety of investments. As well as being asked to invest in the usual types of securities, such as shares and debentures, the public has been asked to invest in contributory mortgages, hire-purchase paper, bills of exchange, and a number of quasi-syndicates. Collapses have occurred mainly in investment in these less usual types of securities – investment that has not yet given rise

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15 Defined in s 2 as meaning "any partnership, special partnership, joint venture, or other unincorporated association of persons established (whether before or after the commencement of this Act) to undertake, with a view to profit or gain, any financial or business scheme, venture, or enterprise".

16 This was also achieved in a roundabout way; the prohibition applied to any person but with an exemption for bodies corporate.

17 (14 December 1977) 416 NZPD 5339.

> to similar duties and responsibilities as apply to the usual types of investment.
>
> The Bill defines securities in a very wide sense, and, generally speaking, it will require commercial entities offering securities to the public to do so by way of a registered prospectus, to appoint an independent person to look after the interests of investors, to keep and disclose adequate financial information, and to be subject to official scrutiny. Precedents for the duties and responsibilities I have just mentioned are to be found in the Protection of Depositors Act 1968, the Syndicates Act 1973, and those provisions of the Companies Act 1955 that relate to prospectuses. The Bill will repeal those enactments and provisions that deal with particular types of entities, and instead will constitute a virtually comprehensive source of statute law on the duties and responsibilities that arise when an entity offers securities to the public.
>
> Put another way, the Bill represents activity-based legislation that will deal with this area of law as a whole, so that there are no inconsistencies in its regulation and development, and, more importantly, it will remove the present opportunity for disreputable promoters to operate in less well regulated areas.

The "financial collapses" referred to by the Minister included the failure of the JBL and Securitibank groups of companies.

[44] Systematic regulation of the offering of investments to the public has its origins in the United States Securities Act 1933. Under that Act (and a large number of state statutes also regulating securities), "security" is defined by reference to a lengthy list of financial instruments, including very significantly, "investment contract". Provincial securities legislation in Canada (most particularly in Ontario) followed (at least broadly) the scheme of the American federal and state legislation and also relied on the same expression, "investment contract". In Australia, the corresponding provisions in the Uniform Companies Act 1961 as adopted by state legislatures addressed the offering to the public of an "interest", the definition of which included "investment contract", which itself was further defined.

[45] The definitions which appear in the New Zealand Act must have been drafted with the American, Canadian and Australian provisions in mind. Indeed some of the language in the eventually enacted definitions may have been borrowed from those provisions.[18] More generally, the New Zealand Act was plainly aimed in at least the

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18 This is helpfully and comprehensively discussed by Matthew Dunning "The Definition of 'Security' for the Purposes of a Securities Act" [1984] NZLJ 71.

same general direction as its counterparts in America, Canada and Australia. As well, and perhaps more significantly, the overall design of the Securities Act appears to have been influenced by the Australian legislation. As discussed by the High Court of Australia in *Australian Softwood Forests Pty Ltd v Attorney-General of New South Wales*,[19] features of this legislation were, on the one hand, extremely broad primary provisions and, on the other, both specific exemptions and the power to provide for more exemptions by regulations – features which discouraged the High Court in *Australian Softwood Forests* from reading down the primary provisions.

The general structure of the Securities Act

[46] If ss 33 and 37 are read just with the definitions which we have set out, their scope would be unacceptably broad. This has been addressed by the legislature in three ways:

(a) the definition of "security" contemplates its supplementation by regulation – supplementation which may either extend or limit its application;

(b) there are a number of exemptions provided for in s 5, including, most relevantly for the purposes of this case, s 5(1)(b) in relation to real property; and

(c) under s 5(5)[20] it was open to the Commission to exempt any person or class of persons, or transaction or class of transactions, from the operation of the Act.

Given this statutory context, we consider that the approach taken by the Australian High Court in the *Australian Softwood Forests* case is directly applicable and that accordingly the primary provisions (ss 33 and 37 and the associated definitions of "security" and "debt security") should, despite their breadth, be read in a way which

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19 *Australian Softwood Forests Pty Ltd v Attorney-General for the State of New South Wales; ex rel Corporate Affairs Commission* (1981) 148 CLR 121.

20 Now repealed.

accords with the ordinary meaning of the words used. In other words, we do not see that breadth as warranting a reading down exercise.

The leading decisions on the scope of the "debt security" definition

[47] The leading decisions are the judgments of the Court of Appeal and the Privy Council in *Culverden Retirement Village v Registrar of Companies*.[21]

[48] *Culverden* concerned a retirement village, the units of which were marketed on terms requiring their repurchase by the operator once they were no longer needed by their purchasers. In issue was whether the repayment obligations of the operator engaged the definition of debt securities on the basis that the operator's repurchase obligations conferred rights upon the original purchasers to be paid money. The appellant operator argued that the definition should be construed as only applying to indebtedness which was in the nature of, or similar to, the obligation to repay money which had been lent to, or deposited with, the debtor.

[49] In the Court of Appeal the argument was recorded and dealt with in this way:[22]

> Mr Judd [QC] for Culverden submitted first that the buy-back provision was not a debt security. The definition of "debt security" is "any interest in, or right to be paid money that is, or is to be, deposited, lent or otherwise owing by any person". He submitted that the words "otherwise owing" should be read as covering only transactions of a similar kind to a deposit or loan. It should be read as coloured by its context, and as referring only to financial transactions involving a money consideration on both sides. Unless so read, he submitted, one would have the absurdity that an ordinary contract for sale and purchase of a dwellinghouse would create a debt security, as the vendor obtains the right to be paid money on settlement.
>
> The definition goes on to state certain transactions which are included and one which is not included. These are of little help in construing the earlier words. We agree that one would not ordinarily expect the term "debt security" to refer to an agreement for the sale and purchase of land. On the other hand, the words "or otherwise owing" are of the widest ambit, and they are not qualified in the definition itself. They are effectively qualified by the provisions of section 5. The scheme of the Act appears to be to cast the net in the widest possible terms, and then to rely on specific exclusions to limit

21 *Culverden Retirement Village v Registrar of Companies* (1996) 1 BCSLR 162 (CA); aff'd [1997] 1 NZLR 257 (PC).

22 At 165–166.

> its scope. An agreement for sale and purchase of a dwellinghouse or of other land is excluded, subject to a stated exception, by s 5(1)(b). We see no reason to read down the wide language of the definition.

[50] The Privy Council was inclined to the same view but resolved the case against the operator on a different basis:[23]

> The appellant submitted that this definition envisages a transaction whereby the consideration on both sides is an obligation to pay or repay money. Their Lordships incline to the view that this is too narrow a reading. But even by this strict criterion this case falls within the definition. The right acquired under the buy-back provision was not granted in isolation. It cannot be equated with the right of a seller under an ordinary contract for the sale of land. It was a right granted to those who signed the sale and purchase agreement. As already noted, the money agreed to be paid by the appellant to the unit holder under the buy-back provision in due course was by way of repayment of money previously paid to the appellant by the unit holder. It was not repayment in the sense of repayment of a loan. But it was repayment in the sense of payment back of the same amount, subject to adjustment for charges and inflation.

The "otherwise owing" issue

[51] Mr Neutze, who argued this aspect of the case for all the developers, accurately analysed *Culverden* as involving two parties, a subscriber (the prospective unit owner) and an issuer (Culverden), a payment by the subscriber to the issuer (for the purchase of the unit) and a "repayment" by the issuer to the subscriber (when the unit was repurchased). On this basis, he maintained that the case is consistent with the respondents' broader argument that the definition of "debt security" is only engaged by an obligation to pay money which is by way of repayment of money earlier paid to the issuer by the subscriber. He thus argued that the principle established by *Culverden* is not applicable to Blue Chip's obligations to reimburse investors in relation to money paid (or payable) to third parties.

[52] We agree with Mr Neutze (at least broadly) as to the ratio of the Privy Council judgment in *Culverden*. But if money "otherwise owing" is not confined to obligations by an issuer to repay money previously advanced (or something like it) by the subscriber to the issuer, it is difficult to see why it should be confined more generally to repayment of money originally paid by the subscriber to the issuer. And

[23] At 260.

despite the narrowness of the ratio of the Privy Council judgment, its tenor, along with the decision of the Court of Appeal in the same case, strongly supports the investors' arguments.

[53] We recognise that there has been some academic criticism of *Culverden*,[24] but we are nonetheless satisfied that the approach taken by the Court of Appeal in that case, and tentatively supported by the Privy Council, is correct.

[54] The legislative history of the Securities Act shows that the words "deposited with" and "lent to" were borrowed from the precursor provisions of the Companies Act 1955 and the Protection of Depositors Act 1968. It is clear that something more must have been intended to be provided for by the phrase "or otherwise owing". How much more is the central issue on this aspect of the case.

[55] On the developers' primary argument, that "something more" is confined to obligations which, while not exactly those of a borrower to a lender, are nonetheless rather like them. This argument does not admit of much more specificity and thus leaves scope for nuanced – how long is a piece of string – arguments as to how much similarity is required before the definition is engaged. As will become apparent, we consider that the obligations of Blue Chip to the investors were indeed "rather like" those a borrower owes to a lender. But rather than proceed on such an impressionistic basis, we prefer to construe the definition by reference to the meaning of the words it uses.

[56] This plain meaning construction is well consistent with the parliamentary history to which we have referred. In this respect, the remarks made by the Minister of Justice on the Bill's introduction give a very clear steer as to the generality with which the definitions were intended to be approached.

[57] Just as the courts in *Culverden* were faced with arguments that a plain meaning approach would result in a catastrophically broad application of the

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24 PG Watts "Company Law" [1996] NZ L Rev 275 and [1997] NZ L Rev 319; Francis Dawson "Securities Regulation" [2002] NZ L Rev 277 at 281 and John Farrar (ed) *Company and Securities Law in New Zealand* (Brookers, Wellington, 2008) at 1016 (where the effect of the Privy Council judgment is, to our way of thinking, misstated).

Securities Act, we too were pressed with a number of arguments which were said to show the allegedly unworkable consequences of construing the definition in accordance with the language actually used. In particular, it was said that the Securities Act would apply whenever some offering of goods or service to the public carried the possibility that the offeror might have to pay money as a result of some defect in those goods or services or if they were not able to be provided.

[58] Instances where such liability might arise include the marketing of real property which if misrepresented may result in a money liability by the vendor to the purchaser. We see the potential for such liability as so much an ordinary incident of transactions involving the sale of real property as to be naturally within the s 5(1)(b) exemption which we are about to discuss. We recognise, however, that the s 5(1) exemptions are not, in themselves, a complete answer to the developers' point. This is because the possibility of civil liability of the kind they postulate is not confined to transactions of the type provided for in the exemptions. Rather, that complete answer is provided by a purposeful but non-technical construction of the definition of debt security. The usual corollary of selling real or personal property or the provision of other services is the acceptance of liability to provide compensation if things go wrong. But a person offering such goods or services to the public cannot sensibly be said to be *offering* compensation rights. So, on the purposive approach which we prefer, straightforward consumer transactions are not caught by the Securities Act concept of what is involved in offering debt securities to the public. On the other hand, on the same purposive approach, the phrase "otherwise owing" must be construed sufficiently broadly to be able to encompass what the Minister of Justice, when introducing the Securities Bill, called "less usual types of securities".

[59] As already foreshadowed, we consider, in any event, that the Blue Chip products were financing in nature, meaning that the money and obligations Blue Chip owed the investors were "rather like" those owed by a borrower to a lender. To put the same proposition in different words, we see the Blue Chip products as providing mechanisms by which Blue Chip sought and obtained financing from the public. Although this conclusion is not critical to our view that the Blue Chip products were debt securities, it warrants brief explanation.

[60] The investors paid or put up money or money's worth and accepted financial obligations to the developers on the basis of promises by Blue Chip that they would:

(a) be reimbursed for their financial outlay; and

(b) receive a return for their outlay and risk.

[61] It is true that they were also buying apartments but under the investment schemes the apartments had a very limited function. Provided all went according to plan, the investors were never to occupy the apartments. Nor were they ever to receive, directly, the rents which were derived from the apartments. And when the apartments were sold on, the investors received either nothing or next to nothing[25] of any capital gain. Instead, for each investor, the apartment was there primarily as a long-stop against the contingency that Blue Chip might not perform. The apartment thus merely provided a measure of security for Blue Chip's performance. And from the point of view of Blue Chip, the role of the investors was, in part at least, to finance the creation of an inventory of apartments which Blue Chip could re-sell in the future. It is unsurprising therefore that the TWL and Icon SPAs allowed the vendor to substitute another unit for the agreed unit if the substituted unit provided a similar rate of return. All in all, we are left in no doubt that the products can be properly regarded as providing finance for Blue Chip whose obligations back to the investors were indeed "rather like" those of a borrower.

[62] It follows that we disagree with the reasons given by the Court of Appeal for concluding that the Blue Chip products were not debt securities.

Was Blue Chip an "issuer"?

[63] In the argument before us, as in both the High Court and Court of Appeal, the developers argued that Blue Chip was an issuer in relation to the PIP and PAC products. Blue Chip's status as an issuer was fundamental to the argument as presented because the s 33(1) and (2) prohibitions apply only to such offers as are made "by or on behalf of an issuer". So if there is no issuer, there could not be a

25 Five per cent in the case of the JVAs.

breach of s 33(1) and (2). And the only party nominated by the appellants as an issuer was Blue Chip.

[64] It will be recalled that for the purposes of a debt security, the "issuer" is a person "on whose behalf any money paid in consideration of the allotment of the security is received." The developers argued that in relation to the PIP and PAC products, no money went to Blue Chip, with the result that it was not an issuer. This argument was not advanced in relation to the JVA product because some of the money put up by the JVA investors did go to Blue Chip.

[65] As it turns out, this whole issue is rendered irrelevant because of our conclusion, to be explained later, that the developers were issuers.[26] But we are, in any event, satisfied that Blue Chip was an issuer in relation to the PIP and PAC products as well as the JVA product.

[66] The idea underlying the PIP and PAC agreements was that Blue Chip would, before or after settlement, take out the investors and in that way be credited (in relation to the developer) with any money paid by the investor. In this admittedly non-technical sense, the payments made by the investors to the developers were received on behalf of Blue Chip. Given the underlying purpose of the Securities Act, we consider that a non-technical approach is the appropriate way to resolve this issue.

[67] The same result can be arrived at in a more roundabout way: "money" is defined as including "money's worth" and the definition of "subscribe" includes "contribute to, whether by way of cash or otherwise". It follows that where the subscription is not in cash but is rather "otherwise" or in "money's worth", anyone who receives all or part of the "otherwise" or "money's worth" benefit is an issuer. It is perfectly clear that Blue Chip received such benefits. The entering into the SPAs by the investors conferred a number of benefits on Blue Chip, facilitating the payment of the underwriting fees and conferring on Blue Chip control over the apartments. In those circumstances we see no difficulty in treating the relevant subscription as encompassing the entering into of the SPAs given that they provided

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26 See [112] and following.

a mechanism by which the investors provided benefits to Blue Chip, which for this reason also was an issuer.

Did the marketing of the JVA product constitute the offering of equity securities to the public?

[68] Equity security is defined in s 2 to mean:

> any interest in or right to a share in, or in the share capital of, a company; and includes—
>
> (a) a preference share, and company stock; and
>
> (b) a security that is declared by regulations to be an equity security for the purposes of this Act; and
>
> (c) a renewal or variation of the terms or conditions of any such interest or right or a security referred to in paragraph (a) or paragraph (b);—
>
> but does not include any such interest or right or a security referred to in paragraph (a) or paragraph (c) that is declared by regulations not to be an equity security for the purposes of this Act

[69] The appellants' argument that the JVA involved an offer of equity securities was dismissed by the Court of Appeal for the following reason:

> [305] But the more substantial difficulty with the appellants' case ... is that there was no offer to the public for subscription in terms of s 33. The JVA provided that the investor was entitled to all the shares in the company to be incorporated and to appoint the directors of the company. The shares were not purchased from Blue Chip or issued by a company that was offering them to the public for subscription. They were issued to the investor by a company incorporated by the investor himself or herself.
>
> (footnotes omitted)

The appellants maintain that this reasoning does not address the argument that what Blue Chip was marketing were the rights to have shares in a joint venture company. That the joint venture companies were apparently formed on the instructions of the investors is, according to the appellants, beside the point.

[70] The appellants' argument on this point is, at least at first sight, logically compelling. What Blue Chip was offering was, inter alia, the right to go into business with it on a joint venture basis. This right was to be given effect in a

number of ways, including the entitlement to be a shareholder, along with Blue Chip, in a company which was to play a particular role in the investment. Looking at what was proposed in this broad way, the detail of the manner in which the joint venture company was formed and its capital subscribed may be beside the point.

[71] That said, we have reservations as to both the substance of the argument and whether it leads anywhere in the context of this case. The joint venture companies were bare trustees for the investors and Blue Chip and their role was thus not particularly material to the way in which the JVA product operated. And if the financial components of what was marketed by Blue Chip (which included the SPAs) did not engage the definitions of "security" and "debt security", it would be difficult to see how the entitlement of the developers to insist on performance of the SPAs would be impeached by a rather technical breach in relation to the shares in the joint venture companies. Accordingly we see no point in reviewing the arguments on this issue in any more detail.

Is the exemption in s 5(1)(b) applicable?

[72] Section 5(1)(b) provides:

> **5 Exemptions from this Act**
>
> (1) Nothing in Part 2 of this Act shall apply in respect of—
>
> ...
>
> (b) any estate or interest in land for which a separate certificate of title can be issued under the Land Transfer Act 1952 ... other than any such estate or interest that—
>
> (i) forms part of a contributory scheme; and
>
> (ii) does not entitle the holder to a right in respect of a specified part of the land for which a separate certificate of title can be so issued ... .

We note that s 5(1)(c) provides a similar exemption in relation to a proprietary right to chattels.

[73] Issues as to the application of s 5(1)(b) arise in two different ways: first as between Blue Chip and the investors; and secondly as between the developers and the investors (on the basis of the developers' contention that the s 5(1)(b) exemption means that their entitlement to enforce the SPAs is not affected by the Securities Act arguments of the investors). In this section of the judgment we are only going to deal directly with the position as between Blue Chip and the investors and we will deal with the developers' particular argument in the next section.

[74] The Court of Appeal concluded that if the marketing of the various products otherwise engaged s 33, s 5(1)(b) would not displace the application of the Act in respect of certain aspects of the various products.[27] Venning J took a different view in the High Court in that he concluded that the s 5(1)(b) exemption was a complete answer to the investors' Securities Act arguments.[28] On this point, we disagree with Venning J and, as well, conclude that the Court of Appeal approach was too narrow.

[75] Section 5(1)(b) operates as an exemption from the general scope of pt 2 of the Act in relation to interests in real estate. But from that exemption there is a further exception in relation to interests, which both form part of a contributory scheme and do not entitle the holder to a right in respect of a specified part of the land for which a separate title can be issued. "Contributory scheme" is defined in s 2 as meaning:

> any scheme or arrangement that, in substance and irrespective of the form thereof, involves the investment of money in such circumstances that—
>
> (a) the investor acquires or may acquire an interest in or right in respect of property; and
>
> (b) pursuant to the terms of investment that interest or right will or may be used or exercised in conjunction with any other interest in or right in respect of property acquired in like circumstances, whether at the same time or not;—
>
> but does not include such a scheme or arrangement if the number of investors therein does not exceed 5, and neither a manager of the scheme nor

27 At [341]–[342], [348]–[349] and [350]–[351].

28 *Greenstone* at [242]–[250] (discussing the mainstream agreement), [269]–[273] (discussing JVAs) and [287]–[290] (discussing the PIP); *Icon* at [231]–[235] (discussing the PIP) and [240] (discussing the PAC product); and *TWL* at [249]–[258] (discussing the mainstream agreement), [277]–[281] (discussing JVAs); and [295]–[298] (discussing the PIP).

> any associated person is a manager of any other such scheme or arrangement.

[76] The definition of "security" is so broad that, in the absence of these exemptions, the advertising for sale of houses would amount to offers to the public of securities. As well, those who drafted the legislation must have known that there had been extensive litigation in the United States as to whether the sales of real property amounted to "investment contracts" so as to be "securities" for the purposes of the federal Securities Act 1933 and its state equivalents. We will refer to this litigation shortly, but it is sufficient for present purposes to note that the starting point under American law is that "the offer of real estate as such, without any collateral arrangements with the seller or others, does not involve the offer of a security."[29]

[77] As is the case with the definition of "debt security", the leading decisions on the application of s 5(1)(b) are the judgments of the Court of Appeal and Privy Council in *Culverden*. For present purposes, it is sufficient to refer to the way in which the exemption was approached by the Privy Council. Their Lordships recorded the appellant's argument in this way:[30]

> The foundation of the appellant's case was a broad submission that the Act is concerned to protect investors, not borrowers ... or purchasers of interests in land or chattels (see s 5). Buyers of units under the sale and purchase agreements acquire the right to have units of land transferred to them, to which their right under the buy-back provisions is merely ancillary. The latter right is merely one of the conditions of the transfer by way of sale.

They responded to this argument as follows:[31]

> Their Lordships accept that the Act was not intended to protect ordinary buyers of land. This is made clear by the exemption in s 5(1)(b). *Their Lordships do not accept that the purchase of a unit in Culverden Retirement Village is an ordinary purchase of land to which the buy-back provision is ancillary.*
>
> To decide whether one right is ancillary to another involves looking for the substance of the overall transaction. Here the unit holder is unable to sell the

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29 The Securities and Exchange Commission issued guidance on this issue (particularly relating to the offer and sale of condominium units) in January 1973, see *Securities Act Release No. 33-5347*, 38 Fed Reg 1735. This release consolidated previous guidance given in *Securities Act Release No. 33-4877* (May 1962) and *Securities Act Release No. 33-4491* (August 1967).

30 At 259.

31 At 259–260 (emphasis added).

> land of which he has bought the freehold. He needs the appellant's consent to let the property. He may use it, that is, he may occupy the town house. Indeed, he is required to occupy it, because if he ceases to do so the buy-back provision is triggered automatically. Moreover, the buy-back provision can be triggered by failure to pay the weekly fees or observe the rules of the village.
>
> In practical terms the substance of this transaction is that in return for a lump sum payment, a buyer acquires two rights: the right to occupy a unit and the right, when his occupation ends, to be repaid the price he paid, adjusted downwards or upwards according to the length of his occupation, the state of the property, the factors built into the inflation adjustment in his particular case, and the movement of the market. The repayment right, far from being ancillary, is a cardinal feature of the transaction. *This being so, the repayment right cannot be sheltered behind the s 5(1)(b) exemption as an unexceptional term ancillary to the purchase of an interest in land.*
>
> Two points are to be noted regarding this analysis. The first is a general point. Financial transactions may be simple or complex. Frequently they involve a bundle of mutual rights and obligations, some to be performed at once and others years later. This does not mean that the Act must apply to the transaction as a whole or not at all. The Act applies to offers of interests or rights which are securities as defined. A single offer may lead to a single transaction containing several components, one or more of which may be within the statutory definition of securities and others not. Separate and quite different securities may be comprised in one contract. The offer of one right in conjunction with other rights and obligations cannot of itself exempt that right from being tested against the statutory definitions.
>
> Nor, furthermore, does it mean that when so tested the right must be considered in isolation from its actual factual and legal setting. When each component in a transaction is being considered, its position within the framework of the transaction as a whole is material and may be crucially important. Any other interpretation of the Act would emasculate its operation.
>
> Secondly, in the present case there is nothing artificial in focusing on the unit holder's right under the buy-back provision as a candidate for the attentions of Part II of the Act. The artificiality here lies in the way the appellant seeks to characterise the transaction as wholly within the s 5(1)(b) exemption, on the basis that the buy-back right is an unexceptional ancillary term to the acquisition of an estate in land, or if it is not, then to look at each element in isolation and disregard the setting in which alone the unit holder's right under the buy-back provision arises.

[78] It could not seriously be suggested that the transactions entered into between the investors and Blue Chip in relation to the apartments (for instance the option arrangements in relation to the PIP and PAC products) involved “the ordinary purchase of land” or that the Blue Chip obligations to the investors in relation to the apartments were in the nature of “an unexceptional term ancillary to the purchase of

an interest in land". It follows that the argument that s 5(1)(b) excludes a Securities Act challenge to the marketing of the Blue Chip products is flatly inconsistent with the approach taken by the Privy Council.

[79] In the United States, a substance-over-form approach has been taken when deciding whether offers of real property are securities. The leading cases are the decisions of the United States Supreme Court in *Securities and Exchange Commission v Howey Co*[32] and *United Housing Foundation Inc v Forman*.[33] Offers of real estate are securities when accompanied by collateral arrangements intended to provide returns based on the efforts of others. This approach has been taken to the sale of land pursuant to schemes involving development for horticultural purposes.[34] As well, the Securities Act has also been applied where apartments are offered for sale in conjunction with rental arrangements:[35]

> ... with emphasis on the economic benefits to the purchaser to be derived from the managerial efforts of the promoter, or a third party designated or arranged for by the promoter, from rental of the units.

[80] The American cases are addressed to the phrase "investment contract", which is one of an extraordinarily long list of expressions comprising the definition of "security" in the 1933 Act. What can be termed the "offer of real estate exception" under that Act does not have an independent statutory basis, but rather has emerged as the courts have teased out the concept of "investment contract". But while the significance of the American cases is thus only contextual it is, nonetheless, appreciable. The underlying purpose of the United States and New Zealand statutes is the same. As well, the American cases show that in terms of securities regulation generally, there was nothing aberrant in the purposive approach generally taken by the Privy Council in *Culverden* and which we propose to apply.

[81] We have already discussed and analysed the role the apartments played in the Blue Chip investment schemes. The reality is that from the point of view of the investor – and assuming of course that all went according to plan – the apartments

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32 *Securities and Exchange Commission v Howey Co* 328 US 293 (1946).
33 *United Housing Foundation Inc v Forman* 421 US 837 (1975).
34 As in *Howey*, above n 32, and *Securities and Exchange Commission v Bailey* 41 F Supp 647 (SD FLA 1941).
35 See the Securities and Exchange Commission's release referred to above at n 29.

were of only peripheral significance. Such profits as the investors could expect to derive were to come substantially from the efforts and substance of Blue Chip. And, as events have shown, the practical ability of the investors to recover their outlays was very dependent on Blue Chip honouring its promises. Those promises were well removed from what could be seen as ancillary to ordinary real property transactions. Rather, in our appreciation, they fell four square within the intended regulatory scope of the Act.

[82] We note that the Court of Appeal considered that some aspects of the promises made by Blue Chip were "ancillary" to the purchase of interests in land and thus protected by the exemption. This was in respect of the right under the JVA to receive interest payments and the right under the PIP to receive option fees. As is no doubt apparent, we disagree. The financial promises made by Blue Chip must be addressed in the way they were intended to be considered by the investors, that is, as a whole. And we think it perfectly clear that as a whole, those promises are not protected by the exemption.

[83] For these reasons we are satisfied that the s 5(1)(b) exemption does not apply.

Do breaches of the Securities Act associated with the marketing of the investment products affect the developers and, if so, to what extent?

Preliminary comments

[84] For the reasons we have given, we are satisfied that Blue Chip's marketing of its investment products was in breach of the Securities Act, on the basis that these investment products were debt securities offered to the public without a prospectus, it was an issuer and the s 5(1)(b) exemption is not applicable. The developers argued that if we were to reach these conclusions, this would not impeach their ability to insist on performance, by the investors, of the SPAs. Their position on this is supported by the judgments of both Venning J[36] and the Court of Appeal.[37] The arguments before us on this aspect of the case covered much ground, including the

[36] *Greenstone* at [114], [159], [309] and [333]–[334]; *Icon* at [106], [163], [260] and [280]–[284] and *TWL* at [116], [153], [328] and [349]–[351].

[37] At [209] and [359]–[368].

operation of the s 5(1)(b) exemption as between the developers and investors, the extent of the knowledge of the developers of the detail of Blue Chip's investment products, whether the actions and knowledge of Blue Chip should be imputed to the developers and, more generally, as to the application of the law of illegal contracts and the extent to which a contract, in itself lawful, might be tainted and rendered unenforceable by reason of associated illegality.

[85] We do not propose to respond to all of these arguments. This is because we consider that this aspect of the case, as with all others, must be determined on the basis of the language used in, and the policy underlying, the Securities Act. As will become apparent, we have concluded that the SPAs are rendered unenforceable by s 37.

A broad analysis of the relationships between the parties

[86] Mr Bryers was the sole director of Icon at the time it entered into the SPAs which are in issue in this appeal. So there can be no question that, through him, Icon was fully aware of the nature of the Blue Chip investment products and how they were being sold. In dispute, however, is the position as to the knowledge of those associated with the other two developers, Greenstone and TWL.

[87] It is common ground that Greenstone and TWL knew that the Blue Chip agents were, as part of their marketing of the apartments, also selling Blue Chip packages. They also knew that these packages included lease arrangements. They must have realised therefore that the investment packages which Blue Chip was marketing included financial promises made by Blue Chip. In each case, however, their knowledge (or at least the information supplied to them) went further than this.

[88] Mr Abel-Pattinson of Greenstone had attended a presentation at which the JVA product was explained by a Mr Miles of Blue Chip. It is perfectly clear that he was aware of the general nature of the product and both Venning J[38] and the Court of Appeal[39] so found.

[38] At *Greenstone*, above n 2, at [127]–[133].
[39] At [137]–[140].

[89] In the case of TWL, Ms Sue Reynolds, the person who liaised with Blue Chip was, on 17 January 2007, sent copies of the PIP agreement and deed of nomination. She also attended a meeting at which she learnt that the PIP was being marketed to "professional investors" and that Blue Chip intended to re-sell the apartments through its normal sales process approximately eight months after settlement. As well, at meetings attended by her and Mr Manning, references were made to the PIP and JVA agreements. Both Venning J[40] and the Court of Appeal[41] concluded that despite this information being supplied, Mr Manning and Ms Reynolds had not taken on board the detail of the products.

[90] So Icon and Greenstone had either complete (in the case of Icon) or substantial (in the case of Greenstone) knowledge of the detail of the investment products. And TWL had been provided with this detail but had not taken it on board.

[91] Another way of looking at the substance of what happened is in terms of whether it would be appropriate to attribute to the developers the actions and knowledge of Blue Chip.

[92] Strictly speaking, Blue Chip was not the agent of the developers in that Blue Chip was not authorised by the developers to act on their behalf so as to affect their (legal) relationship with third parties;[42] this because they were not authorised to commit the developers contractually. Blue Chip was, however, the "agent" of the developers in the rather different sense of acting on their behalf in the marketing of the apartments. In this respect, their role in relation to the developers was very similar, although not identical, to that of real estate agents in relation to the vendors of property whose task is to solicit offers. It will be recalled that the definition of "offer" includes both "an invitation" and "any proposal or invitation to make an offer". Blue Chip was soliciting offers and was doing so "on behalf of" (the phrase which appears in s 33(1) and (2)) the developers.

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40 At *TWL*, above n 2, at [127]–[132].
41 At [150]–[152].
42 See Peter Watts (ed) and FMB Reynolds *Bowstead and Reynolds on Agency* (19th ed, Sweet & Maxwell, London, 2010) at [1-001].

[93] A real estate agent (unlike Blue Chip in the present case) is usually able to accept a deposit on behalf of the vendor and, to that limited extent, is an agent in the strict sense of the term. But the liability of a vendor for the actions of a real estate agent is not controlled by whether the deposit is to be paid to the real estate agent, a point which is illustrated by the leading Australian case, *Colonial Mutual Life Assurance Society Ltd v Producers and Citizens Co-operative Assurance Co of Australia Ltd*.[43] In issue in that case was whether an insurance company was vicariously responsible for defamatory remarks made by its canvassing agent. He was strictly only an agent in relation to his authority to accept premiums. Otherwise, he was an independent contractor. The canvassing agent's ability to accept premiums was logically irrelevant to whether the insurance company was vicariously liable for the defamatory remarks he made. Indeed the judgment of the Court, in holding the insurance company vicariously liable, proceeded on the basis that the canvassing agent had been its representative. Interestingly, Gavan Duffy CJ and Starke J chose to use an apparent oxymoron when describing the canvassing agent as:[44]

> an agent of the defendant in the nature of an independent contractor ...

It is by parity of reasoning that misrepresentations by a real estate agent will usually be attributed to a vendor.

[94] Often enough where attribution is in issue, the only ability of the "agent" to affect the principal's legal relationships with third parties is with regard to the actions in respect of which vicarious liability is asserted. So in the English case of *Morgans v Launchbury* – a case which concerned the liability of the owner of a car for the actions of a bailee – Lord Wilberforce noted that: [45]

> I accept entirely that "agency" in contexts such as these is merely a concept, the meaning and purpose of which is to say "is vicariously liable," and that either expression reflects a judgment of value – respondeat superior is the law saying that the owner ought to pay.

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43 *Colonial Mutual Life Assurance Society Ltd v Producers and Citizens Co-operative Assurance Co of Australia Ltd* (1931) 46 CLR 41.

44 At 46.

45 *Morgans v Launchbury* [1973] AC 127 (HL) at 135.

And Gleeson CJ commented in *Scott v Davis*:[46]

> Lord Wilberforce made the point that to describe a person as the agent of another, in this context, is to express a conclusion that vicarious liability exists, rather than to state a reason for such a conclusion.

[95] As those quotations indicate, policy considerations come into play. This was made clear by the Privy Council in *Meridian Global Funds Management Asia Ltd v Securities Commission*,[47] a case concerned with whether the knowledge of a Mr Koo of the acquisition of shares he made on behalf of Meridian, albeit in fraud of Meridian and corruptly, should be attributed to Meridian for the purposes of imposing liability to a penalty for breach of a regulatory disclosure regime. In a judgment delivered by Lord Hoffmann, the Privy Council held that:[48]

> The policy of s 20 of the Securities Amendment Act 1988 is to compel, in fast-moving markets, the immediate disclosure of the identity of persons who become substantial security holders in public issuers. Notice must be given as soon as that person knows that he has become a substantial security holder. In the case of a corporate security holder, what rule should be implied as to the person whose knowledge for this purpose is to count as the knowledge of the company? Surely the person who, with the authority of the company, acquired the relevant interest. Otherwise the policy of the Act would be defeated. Companies would be able to allow employees to acquire interests on their behalf which made them substantial security holders but would not have to report them until the board or someone else in senior management got to know about it. This would put a premium on the board paying as little attention as possible to what its investment managers were doing. Their Lordships would therefore hold that upon the true construction of s 20(4)(e), the company knows that it has become a substantial security holder when that is known to the person who had authority to do the deal. It is then obliged to give notice under s 20(3). …
>
> But Their Lordships would wish to guard themselves against being understood to mean that whenever a servant of a company has authority to do an act on its behalf, knowledge of that act will for all purposes be attributed to the company. It is a question of construction in each case as to whether the particular rule requires that the knowledge that an act has been done, or the state of mind with which it was done, should be attributed to the company. Sometimes … it will be appropriate. Likewise in a case in which a company was required to make a return for revenue purposes and the statute made it an offence to make a false return with intent to deceive, the Divisional Court held that the mens rea of the servant authorised to

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46 *Scott v Davis* [2000] HCA 52, (2000) 204 CLR 333 at 339.
47 *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 3 NZLR 7 (PC).
48 At 16.

> discharge the duty to make the return should be attributed to the company: see *Moore v I Bresler Ltd* [1944] 2 All ER 515. On the other hand, the fact that a company's employee is authorised to drive a lorry does not in itself lead to the conclusion that if he kills someone by reckless driving, the company will be guilty of manslaughter. There is no inconsistency. Each is an example of an attribution rule for a particular purpose, tailored as it always must be to the terms and policies of the substantive rule.

[96] The importance of policy is also illustrated by the Supreme Court decision, *Dollars & Sense Finance Ltd v Nathan*.[49] In this case, the solicitor (a Mr Thomas) acting for the lender had asked the borrower (Rodney Nathan) to obtain the required signatures from the guarantors (who were to be his parents). Rodney obtained his father's signature but simply forged his mother's signature. The guarantee was incorporated into a mortgage and this was later registered. In issue was whether the security interest apparently conferred by the mortgage was defeated on the basis that the fraud of Rodney should be attributed to the lender, Dollars & Sense. Obviously Dollars & Sense had not authorised Rodney to forge his mother's signature. In that sense his actions were plainly unauthorised and in his own interests and not in the interests of Dollars & Sense. On the other hand, he had been authorised to obtain a registrable security which is, in a sense, what he did. In issue was which of these formulations provided the appropriate basis for deciding the case, a question which ultimately involved a policy judgment:[50]

> The tenor [of the relevant authorities] is that someone who creates an agency in which there is a risk of improper behaviour by an agent (or, as in this case, by someone entrusted with a sub-agency) should expect to bear responsibility where that risk eventuates and loss is thereby caused by the agent to a third party. The nature of that risk and the extent of the liability will depend upon the nature and scope of the agency. In this case, even without the benefit of hindsight, a moment's reflection exposes the risk of a borrower's being tempted to mislead his guarantors or to exercise undue influence over them or, at the worst, to forge their signatures. Forgery was a peril which was avoidable if Mr Thomas had not put Rodney in a position where it was left to him to obtain the necessary signatures. It is not therefore at all unreasonable for Rodney's forgery to be regarded as an act done in the course of the agency. All the more so is this reasonable where it can be said that [Dollars & Sense] was in fact benefiting from the fraud. Obviously, the forgery played a material part in enabling [Dollars & Sense] to become registered as mortgagee. By registering the forged document it obtained the status of legal mortgagee. It is seeking to retain that advantage by means of retaining its registration and exercising a power of sale under the mortgage.

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49 *Dollars & Sense Finance Ltd v Nathan* [2008] NZSC 20, [2008] 2 NZLR 557.
50 At [48] (footnotes omitted).

> Where a third party is affected by the agent's forgery a principal should not be allowed to deny the agency in order to take the benefit of the registration of the forged document.

[97] Where imputation is in issue, there are usually different ways of describing the functions of the agents in relation to their principals and the present case is no exception. On one approach, those functions were simply to produce buyers of the apartments so that anything else the Blue Chip agents did (for instance in terms of selling Blue Chip products at the same time to the same people) was not on behalf of the developers. Another of way looking at the situation is that the developers appointed the Blue Chip agents to market the apartments and knew that this would occur in conjunction with the marketing of Blue Chip products and, in that broad sense, authorised the Blue Chip agents to do exactly what they did do, that is market the apartments through the use of the Blue Chip products.

[98] Which of these two views provides the more appropriate basis for deciding the case, in the end, comes down to an assessment which is controlled by the policy of the Securities Act, rather than the detail of the formal documents by which the developers sought to insulate themselves from the legal consequences of the actions and representations of the Blue Chip agents.

[99] As already explained, Icon and Greenstone knew of either the detail or at least the substance of the investment products which were being marketed and by instructing Blue Chip to market the apartments in conjunction with those investment products, they can, therefore, fairly be regarded as having authorised Blue Chip to do exactly that. TWL was told of the detail of the products too, albeit that the individuals who received this information apparently did not digest it. But irrespective of what TWL was told (or took on board), the knowledge and actions of Blue Chip can fairly be attributed to it given the principles applied in *Meridian* and *Dollars & Sense*.

[100] If Blue Chip had retained the development sites and had developed the apartment buildings itself, it might have funded the developments using investment products which would have been practically identical to those involved in the present case. In such circumstances, it is perfectly clear that the SPAs would have been

unenforceable by reason of s 37. The situation just postulated is in fact very much what happened with the Icon development (in that all the SPAs were entered into before the shares in Icon were sold on). In the case of the Icon apartments, it is difficult to see how it would be reconcilable with policy for the impact of s 37 to be avoided by the simple device of using separate companies for different components of a single integrated financial product. And in the case of the other two developments, it is equally difficult to see why the end result should be different because of the interpolation of third party developers who either knew the nature of the investment products which Blue Chip was marketing or to whom that knowledge (along with the actions of Blue Chip) can fairly be attributed.

The operation of s 37(1) and (4)

[101] Section 37 provides:

> **37 Void irregular allotments**
>
> (1) No allotment of a security offered to the public for subscription shall be made unless at the time of the subscription for the security there was a registered prospectus relating to the security.
>
> ...
>
> (4) Any allotment made in contravention of the provisions of this section shall be invalid and of no effect.

[102] From the view point of the developers, the SPAs were independent of the investment products sold by Blue Chip and they did their best to make that clear in both their dealings with Blue Chip (by denying it the status of being their agents) and in the SPAs signed by the investors (with whole agreement clauses and disavowal of responsibility for the actions or representations of Blue Chip's sales force). As both the High Court and the Court of Appeal held,[51] the SPAs were neither legally nor practically dependent on performance by Blue Chip of its obligations under the associated agreements.

[103] We accept that the developers were perfectly entitled to insulate themselves from the legal consequences of misrepresentations and non-performance by Blue

[51] Above ns 36–37.

Chip. What they could not do, however, is contract out of the Securities Act. For this reason, the appropriate Securities Act categorisation of the actions of the developers and Blue Chip is not controlled by the way in which they were described in the contractual documents.

[104] From the point of view of the investors, the Blue Chip products which they acquired were inextricably linked to the SPAs they signed. This is because the Blue Chip products simply could not work independently of the SPAs. This means that the SPAs and the Blue Chip investments products were integrated packages. This is not affected by the precise order in which the various agreements were entered into, in particular whether the SPA agreement was completed before the JVA, PIP or PAC, providing they occurred at practically the same time and in circumstances where the investor and Blue Chip intended them to operate together. Given the consumer protection focus of the statute, we see this consideration as dominant.

[105] As we have explained, the investors subscribed by, inter alia, committing themselves to the SPAs. By doing this and by making the payments required under the SPAs, they contributed to Blue Chip's investment scheme both "otherwise" and "by way of cash". Those cash payments were to Blue Chip's advantage, as we have explained which, along with the money's worth contribution to Blue Chip represented by the execution of the SPAs, resulted in Blue Chip becoming an issuer. Thus the ordinary language of the definitions supports the conclusion that the subscriptions in this case encompass the actions of the investors in entering into the SPAs. The promises and payments made by the investors to the developers were pursuant to, and in that sense part of, the consideration for the promises made by Blue Chip. This supports the view that the subscriptions which were invalidated by s 37(4) included the contractual commitments of the investors to the developers and the payments the investors made pursuant to those commitments. Although there is no New Zealand authority directly on point,[52] we note that a similar conclusion was

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[52] *DFC Financial Services Ltd v Abel* [1991] 2 NZLR 619 (HC) and *Abbott v UDC Finance Ltd* [1992] 1 NZLR 405 (CA) are distinguishable because the "other" contracts were not so closely integrated into the allotments and thus could not be seen as part and parcel of the "subscription" by the vendors.

reached, in at least broadly similar circumstances, by the Court of Appeal of New South Wales in *Hurst v Vestcorp Ltd*.[53]

[106] Relying on the judgment of the Privy Council in *Christchurch Pavilion Partnership No 1 v Deloitte & Touche Tohmatsu Trustee Co Ltd*,[54] the respondents maintained that subscriptions must be in the form of money and cannot consist of contractual commitments. We disagree. What was said in that judgment was referable to the particular facts of the case and was focussed on s 37(2).[55] But in s 2, "subscribe" is defined as including purchasing or contributing to, "whether by cash or otherwise".

[107] Our conclusion is, accordingly, that s 37(4) invalidates the SPAs.

[108] We should emphasise that the conclusion just reached applies to those cases where the SPAs were executed at the same time as, or after, the corresponding Blue Chip investment product agreements were entered into. There is at least one instance where this was not the case in that the SPA was entered into substantially before the agreement between the investor and Blue Chip was executed. In respect of this instance (and any similar instances), there are obvious difficulties with the argument that the entering into of the SPA represented the subscription for the security. But given that the issue was not addressed in this way in the High Court or Court of Appeal, we think it best to remit the issue to the High Court for determination.

[109] Counsel for the respondents challenged the entitlement of the appellants to advance the argument that the SPAs were unenforceable as part of the subscription for the securities. Contrary to that argument we consider that the appellants' pleadings did encompass the point. We accept, however, that the detail of the arguments advanced in this Court by Mr Campbell for the appellants was somewhat different from those advanced in the High Court and Court of Appeal. To the extent that this approach is new, we see no prejudice to the developers; this because all it involves is applying the Securities Act definitions to facts which are not in dispute.

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53 *Hurst v Vestcorp Ltd* (1988) 12 NSWLR 394 (CA).

54 *Christchurch Pavilion Partnership No 1 v Deloitte & Touche Tohmatsu Trustee Co Ltd* [2002] UKPC 4, [2002] 3 NZLR 289.

55 At [20].

The s 5(1)(b) exemption

[110] The investors are directly challenging enforcement of what, on their face, look to be reasonably orthodox agreements for the sale and purchase of apartments which were being sold off the plans. At first sight, therefore, the transactions between the developers and the investors might be thought to fall four square within the s 5(1)(b) exemption.[56] Such an approach, however, ignores the bigger picture:

(a) The investors subscribed for the securities which Blue Chip was issuing by, inter alia, entering into the SPAs and, as we have explained, the operation of the Blue Chip products (which we have held to be debt securities) were inextricably associated with the SPAs.

(b) Icon and Greenstone knew either the detail (in the case of Icon) or at least the substance (in the case of Greenstone) of the investment products which Blue Chip was marketing.

(c) The knowledge of Blue Chip and its actions (which included marketing the apartments and investment products as integrated packages) is to be attributed to each of the developers.

(d) So the developers were parties to the actions of Blue Chip and its sales force with full attributed knowledge of the substance and detail of the Blue Chip products and that those products and the SPAs were marketed as integrated financial packages.

On this basis, we are satisfied that the SPAs do not fall within the exemption.

56 The apartments were sold off the plans and, accordingly, at the time the agreements were entered into, certificates of title for each apartment were not available. The investors, however, did not argue that this meant that the s 5(1)(b) exemption was inapplicable. Presumably this is because they proceeded on the basis that by the time the agreements were to be enforced, such certificates would be available.

Tainting by illegality

[111] We note the alternative approach adopted by Tipping J which proceeds on the basis that the developers are liable as accessories to Blue Chip's breaches of the Securities Act and that this results in the illegality of the SPAs. We accept that this may provide an alternative way in which relief is available to the investors but prefer to approach the case within the confines of the Securities Act.

The developers as issuers

[112] To this point our reasons follow broadly the arguments advanced by Mr Campbell in this Court. After the hearing, it occurred to us that s 37(5) provided an alternative approach. This subsection provides:

> Where subscriptions for securities are received by or on behalf of an issuer, but, by virtue of this section, the securities may not be allotted, or for any reason the securities are not allotted, the issuer shall ensure that—
>
> ...
>
> (b) the subscriptions, together with such interest (if any) as has been earned thereon, are repaid to the subscribers as soon as reasonably practicable.

This subsection could apply directly to the developers only if they were issuers. And despite the case not having been argued on this basis, it seemed to us to be well arguable that they were issuers:

(a) The consideration provided by the investors for the allotment by Blue Chip of the securities included entering into the SPAs and any payments made under them.

(b) The developers thus received what was provided by the investors to Blue Chip as consideration for the allotments, in the form of money (being deposits) and money's worth (in the form of the obligations under the SPAs), and were thus "issuers" within the s 2 definition.

(c) The SPAs (along with any payments made by the investors to the developers under them) were subscriptions within the meaning of the s 2 definition.

(d) Applying s 37(5) to the circumstances as they now are, the developers must repay any money received and must cancel the SPAs or are otherwise disqualified from enforcing them.

[113] Because this argument had not previously been advanced, we invited the parties to make submissions as to both whether it was appropriate to deal with the argument and, as well, as to its merits. We were strongly urged by the respondents to put the argument to one side, given that the appellants did not advance it earlier. They claimed that this resulted in prejudice to the respondents' position, which was associated with both the conduct of the trial and broader considerations such as litigation strategy (including possible settlement) and whether their directors ought to have been separately advised. We see nothing material in the prejudice argument. Having reached the point where we have already concluded that the SPAs are caught by s 37(4), the question whether the developers were issuers involves merely the application of the law to facts which are not materially in dispute (given the findings we have already made). In any event, as is already explained, the appellants have succeeded on the appeal on the points they did argue and for the moment we are not persuaded that the respondents will necessarily be worse off under s 37(5) than they are under s 37(4).[57] Concerns about litigation strategy (along the lines of, "We might have settled earlier if only the point had been taken earlier") (a) do not involve prejudice of a kind which is material in the present context (that is forensic prejudice resulting from the possibility that the other party may have led other evidence or otherwise conducted its case differently if the point had been taken earlier) and (b) are not very persuasive anyway, given the firm stance taken by the developers to the upstream issue whether Blue Chip was in breach of the Securities Act.

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57 There may be a difference as to liability to refund deposits but at least for the moment, we are not persuaded that the investors' success under s 37(4) would not result in the recovery of deposits. Liability under s 37(5) triggers secondary liability for the directors of the developers under s 37(5) but the investors could perhaps pursue such liability in separate proceedings and in any event, in practical terms, such liability would only arise if the developers are not able to make any required refunds.

[114] The absence of tangible prejudice is not in itself a justification for allowing a point to be taken so late in the piece, and this perhaps might be thought to be all the more so given that the appellants have succeeded anyway. On the other hand, there is likely to be further litigation (both in the context of the present proceedings because the case will have to be remitted to the High Court for final orders and possibly as well, by investors who are not parties to the present case). Given this, we think that consideration of the issuer point is warranted.

[115] The respondents' arguments addressing the merits of the issuer point are closely focused on the details of the contractual arrangements between (a) the investors and Blue Chip on the one hand and (b) the investors and the developers, on the other hand. These arguments are largely premised on the contention that the definition of "issuer" encompasses only what may be provided by the investor to the issuer in consideration for an allotment by the issuer to the investor. Here "the allotments" were made by Blue Chip, with the result that the promises and payments by the investors to the developers where not in consideration of allotments made by the developers. It was also said that if the investor had entered into an SPA agreement before the completion of formalities associated with the Blue Chip product (as would appear usually to have been the case with the JVAs and is what was contemplated by the PACs), the entry into the SPA preceded the allotment of the security and therefore could not be consideration for it.

[116] Usually the same person will be both the issuer and the offeror of securities. But this is not necessarily always going to be the case. If it were, there would be no need to provide separately for offerors and issuers. As well, there is no requirement for the issuer to be the person who is the "allotter" of the securities. If this had been intended, "issuer" would have been defined accordingly rather than in terms of who receives the money. In the result, the Act provides separately for "offerors", "issuers" and "allotters".[58] Once this is appreciated, the appropriateness of a strictly contractual approach to what is relevantly "consideration" falls away as do arguments as to past consideration.

[58] See Securities Act 1978, s 6.

[117] The respondents also relied on the initially conditional nature of the SPAs associated with the JVAs and PIPs meaning that the deposits were paid to the developers' solicitors as stakeholders with the result that the developers were not unconditionally entitled to them when the JVAs were entered into, and also the conditionality of the PIP agreements.[59] Neither argument is persuasive. The contractual commitments of the investors under the SPAs, conditional or not, and the payments of deposits (which resulted in the developers having conditional interests in them) were, to our way of thinking, sufficient to amount to subscriptions. And the argument as to the conditionality of the PIPs ignores both the commercial and probably the legal reality that Blue Chip would ensure that the developers did not execute the SPAs until it was itself committed to the PIP agreement as discussed in [12] above.

[118] The respondents also suggested that a broad approach to who could be an "issuer" would have unintended and unacceptable consequences, for instance encompassing all those who might receive payments funded by the investors or be the beneficiaries of promises they made, including in the present case, financiers, valuers, and the suppliers of the furniture packs. We see these concerns as misplaced. The definition of "issuer" includes only those on "whose behalf" subscriptions are received, which, in the context of the present case seem to us to be confined to Blue Chip and the developers. It is not language which easily encompasses those whose trade debts, incurred in relation to the supply of goods and services to the enterprise, are paid from money received by an issuer.

[119] Accordingly, on the basis of the considerations mentioned in [112] and our rejection of the opposing arguments, we are of the view that the developers were issuers.

Sections 37AH, 37AJ and 37AL

[120] These sections provide:

> **37AH When court may make relief order in respect of section 37**

[59] See [12] above.

(1) The court may in the course of any proceedings, or on the application of the issuer under this section, make a relief order in respect of the application of section 37 to the allotment of a security if the court considers that it is just and equitable to do so.

(2) An order may be made under this section regardless of whether the contravention of section 37 occurred before or after this section comes into force.

(3) In determining whether to make a relief order under this section, the court must have regard to—

(a) all of the circumstances relating to the allotment of the security; and

(b) the nature and seriousness of the contravention of section 37; and

(c) whether the contravention has materially prejudiced the interests of the subscriber; and

(d) whether the subscriber has disposed of the security to any other person; and

(e) any other matters that the court thinks fit.

37AJ Other orders that court may make in relation to relief orders under section 37AH or section 37AI

If the Court makes a relief order under section 37AH or section 37AI, the Court may—

(a) make the relief order subject to any terms and conditions that it thinks fit if the contravention of section 37 has materially prejudiced the interests of the subscriber; and

(b) in respect of a security, order the issuer to pay compensation to—

(i) the subscriber for any loss or damage suffered by the subscriber that is caused by the contravention of section 37; and

(ii) any person who has, at any time, been a security holder in relation to the security for any loss or damage suffered by the person that is caused by the contravention of section 37; and

(c) grant any mandatory, restrictive, or prohibitory injunction that the court thinks fit; and

(d) make an order for any consequential relief that the court thinks fit, unless the court makes the relief order under section 37AI.

37AL Other proceedings for relief in respect of section 37

(1) This section applies—

(a) to all proceedings commenced after this section comes into force that relate to an allotment of a security made in contravention of section 37; and

(b) to all proceedings that have not been finally disposed of by the court of first instance before this section comes into force that relate to an allotment of a security made in contravention of section 37.

(2) The Court must not, in respect of an allotment of a security made in contravention of section 37, make any order or declaration, including an order or declaration in respect of moneys payable, relief, validation, restitution, compensation, variation of a contract, or relief of a contract in whole or part or for any particular purpose, other than any of the following orders:

(a) any order in accordance with any of the provisions of sections 37AA to 37AK, this section, and sections 37B to 37G:

(b) any order or direction in relation to a matter of procedure:

(c) any order as to costs:

(d) any order to require the repayment of any subscriptions or interest under section 37(5) or (6):

(e) any order in relation to proceedings under section 59:

(f) any order in relation to proceedings under section 60(2).

...

(4) Subsection (5) applies if—

(a) proceedings have been commenced to require the repayment of subscriptions or interest under section 37(5) or (6) in relation to the allotment of a security; and

(b) an application has been made for a relief order in relation to the security under 1 or more of the following provisions:

(i) section 37AC:

(ii) section 37AH:

(iii) section 37AI.

(5) The Court must, on the application of the issuer, order that the proceedings to require the repayment of subscriptions or interest under section 37(5) or (6) be stayed until after the determination of the application, or applications, for a relief order unless the application, or applications, for a relief order—

(a) is, or are, frivolous or vexatious; or

(b) is, or are, an abuse of the process of the court.

[121] On a first reading, s 37AL might be thought to be applicable to the present proceedings; this because they might be thought to “relate to an allotment of a security made in contravention of section 37”. If this were correct, it would mean that the orders which can be made are confined to those specified in s 37AL(2). But if this were so, it would mean that s 37(4) and (5) would be incapable of direct enforcement, something which is plainly not contemplated at least in the case of s 37(5) by s 37AL(5). And in any event, the relevant legislative history makes it clear that s 37AL was intended to address concerns as to whether the Illegal Contracts Act 1970 could be relied on by issuers[60] and that it was not intended to preclude direct enforcement of s 37(4) and (5) by investors.

Disposition

[122] Our judgment has resolved issues which were before us but they do not address (because we did not hear argument on) the practical implications of our conclusions which we think can best be worked through in the High Court.

[123] The result is that:

(a) The appeals are allowed.

(b) The SPAs executed at the same time as, or after, the corresponding Blue Chip investment product agreements were entered into are declared to be unenforceable under s 37 of the Securities Act 1978.

(c) The High Court is to determine whether SPAs, entered into before the corresponding Blue Chip investment products were executed, were subscriptions for securities.

(d) The cases are otherwise generally remitted to the High Court to make such further orders as may be consistent with this judgment.

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60 The relevant sections were inserted in the Act by s 12 of the Securities Amendment Act 2004. Their underlying purpose is apparent from (a) Supplementary Order Paper 2003 (152) Business Law Reform Bill 2003 (56–2), (b) Business Law Reform Bill (56–2) (select committee report) and (c) second reading speech of the Hon Rick Barker (on behalf of the Minister of Commerce) (23 March 2004) 616 NZPD 11898.

(e) The respondents are to pay the appellants costs of $75,000 and usual disbursements.

(f) Costs in the High Court and Court of Appeal are to be as determined by those courts.

TIPPING J

Introduction

[124] I agree with William Young J for the reasons he gives that Blue Chip offered debt securities to the public in contravention of s 37 of the Securities Act 1978 and that the offer was not exempted by s 5. Once that point is reached it is necessary to consider whether these conclusions result, as the appellants contend, in the sale and purchase agreements between themselves (the investors) and the developers becoming unenforceable. There are two possible routes to that conclusion. The first is that this consequence follows from the language of subss (4) and (5) of s 37. The second is that the consequence follows as a result of the common law doctrine of tainting. I will discuss the issues in that order.

The statutory route

[125] Any allotment made, as here, in contravention of s 37 is invalid and of no effect (subs (4)). If subscriptions are received by or on behalf of an issuer, but the securities subscribed for may not be allotted, the issuer must ensure that the subscriptions are repaid to the subscribers (subs (5)). The concept of subscription is defined to include purchase and contribution whether by way of cash or otherwise.[61] In effect, therefore, subscription involves the provision of any form of consideration for the allotment. In this case the investors, as subscribers, provided consideration for the allotment which included becoming bound to purchase the apartments from the developers. The concept of repaying subscriptions when an allotment cannot be made involves returning any consideration provided by the subscriber. In present

[61] See the definition of "subscribe" in s 2(1).

circumstances that must mean releasing the subscribing investors from their sale and purchase obligations. Blue Chip cannot do that. The question is whether the developers are obliged to release the investors by virtue of subs (5). That turns on whether the developers were also issuers of the securities of which the sale and purchase agreements formed a necessary and integral part.

[126] The language of subs (5) is such that there may be more than one issuer of a security. The singular noun "issuer" is capable in context of including the plural. The context certainly doesn't exclude that normal construction.[62] The use of the indefinite article in the expression "an issuer" does not, again in context, imply that there can only be one issuer. The definition of issuer, leaving aside irrelevant words, is "the person on whose behalf any money paid in consideration of the allotment ... is received". The word "money" is defined to include money's worth.[63] Because of the interrelationship between the debt securities and the sale and purchase of the apartments,[64] the money's worth supplied by the investors to the developers was in consideration of the allotment. That money's worth was in the form of their contractual commitment to buy the apartments. The developers received that money's worth and hence come within the definition of an issuer.

[127] I have considered whether the word "issuer" in s 37(5) should implicitly be restricted to a person who offers securities to the public. But the offeror and the issuer need not necessarily be the same person. There is no basis in s 37 to justify any implicit restriction being placed on the statutory definition of the word "issuer". Because the developers were issuers within the meaning of s 37(5) they must ensure that the investors' subscriptions are repaid. As we have seen, that means they must release the investors from their contractual obligations under the sale and purchase agreements. Those agreements must therefore be regarded as unenforceable by the developers against the investors.

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62 See s 33 of the Interpretation Act 1999.
63 See s 2(1).
64 Discussed more fully below.

The doctrine of tainting

[128] Despite my conclusion on the point just discussed, it is desirable to consider whether the doctrine of tainting can also be invoked by the investors so as to render their contracts with the developers unenforceable. The point was fully argued and, on my view of the matter, represents an alternative route to the conclusion sought by the appellants. The doctrine of tainting applies when one contract (the collateral contract) is rendered unenforceable by reason of its being tainted by the illegality and unenforceability of another contract (the primary contract). I will first examine the common law on the subject and then consider whether the Illegal Contracts Act 1970 affects the position in New Zealand.

[129] The issue arises when the collateral contract, viewed in isolation of the primary contract, is not itself unenforceable for illegality. But in some cases the collateral contract is so tainted by its association with the illegality of the primary contract that the courts will decline to enforce it. The primary contract in the present case is the contract between the investor and Blue Chip. The collateral contract is the contract between the investor and the developer, namely the sale and purchase agreement in respect of the apartment in issue. The primary contract is invalid and of no effect by dint of s 37(4) of the Securities Act. What is in issue is the enforceability of the collateral sale and purchase agreement in the light of the illegality of the primary contract.

[130] Leading contract law textbooks recognise that a collateral contract may be so tainted by the illegality of the primary contract as to become unenforceable. Anson says that a transaction which is collateral to an illegal agreement may be affected by taint of illegality.[65] Cheshire Fifoot & Furmston say that a subsequent or collateral contract which is "founded on or springs from" an illegal transaction is itself illegal

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65 Jack Beatson, Andrew Burrows, and John Cartwright *Anson's Law of Contract* (29th ed, Oxford University Press, New York, 2010) at 432, citing *Heald v O'Connor* [1971] 1 WLR 497 (a tainted guarantee) and *Fisher v Bridges* (1854) 3 E & B 642, [1854] 118 ER 1283 (deed securing payment for land conveyed for illegal purpose unenforceable).

and void.[66] Treitel states that collateral transactions may be "infected" with the illegality of a principal contract if they help a person to perform an illegal contract.[67]

[131] Burrows, Finn and Todd say that a contract may be tainted by illegality if it is designed to assist or promote a different contract which is in breach of a statute.[68] In Australia, Willmott states that where a contract is illegal it is possible for that illegality to taint a wider scheme or enterprise of which it forms part. If that is so, the same consequence, that is unenforceability, applies to each part of the scheme. The authors add that the question is whether the illegal dealing was an integral part of the whole arrangement entered into, which could not have been performed without the illegal dealing.[69] It is apparent therefore that the existence of a common law doctrine of unenforceability by tainting cannot be doubted. As Megarry J said in *Spector v Ageda*, illegality may be contagious.[70]

The Illegal Contracts Act

[132] I do not consider the Illegal Contracts Act affects the common law doctrine of tainting. The definition of an illegal contract in s 3 of the Act refers only to the primary contract. It does not extend to a collateral contract that becomes unenforceable by dint of the doctrine of tainting. The fundamental premise of the Act is that an illegal contract is of no effect. The court may, however, grant relief in any of the ways specified in s 7. The court may validate an illegal contract and an application for validation may be made by any person where it is material for that person to know whether that form of relief will be given. Hence a party to a collateral contract may seek validation of the primary contract and, if validation is granted, the taint that would otherwise have affected the collateral contract will be removed.

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66 M P Furmston *Cheshire, Fifoot & Furmston's Law of Contract* (15th ed, Oxford University Press, New York, 2007) at 503.

67 Edwin Peel *Treitel: The Law of Contract* (13th ed, Sweet & Maxwell, London, 2011) at [11-166].

68 John Burrows, Jeremy Finn and Stephen Todd *Law of Contract in New Zealand* (4th ed, LexisNexis New Zealand Ltd, 2012, Wellington) at [13.5].

69 Lindy Willmott, Sharon Christensen and Des Butler *Contract Law* (2nd ed, Oxford University Press, Melbourne, 2005) at [18.290].

70 *Spector v Ageda* [1973] Ch 30 (Ch) at 42.

[133] Section 37(4) of the Securities Act does not expressly make an allotment in contravention of the section illegal. It makes an allotment invalid and of no effect. Subsection (5) provides that all subscriptions must then be repaid. However, s 59 of the Securities Act makes it an offence, subject to stated defences, to be involved in the issue of securities to the public in contravention of s 37. Express provision is now made in the Securities Act for relief orders. That was done by the 2004 amendment which inserted ss 37AA to 37G into the principal Act.

[134] The inapplicability of the Illegal Contracts Act to tainted contracts is also consistent with s 5 of that Act which provides that a contract lawfully entered into (which the primary (allotment) contract here was not) does not become illegal *or* unenforceable because its performance is in breach of any enactment, unless the enactment expressly so provides or its object clearly so requires.

[135] Two points emerge from this. For the purposes of the Illegal Contracts Act, illegality and unenforceability are different concepts but, in any event, both the text and object of the Securities Act clearly require unenforceability of the primary contract, albeit now subject to the relief order regime. Relief against non-compliance with s 37 may be granted in the course of any proceeding or on the application of an issuer. Hence if the developers' sale and purchase agreements are found to be unenforceable by tainting, they may in the course of these proceedings seek relief pursuant to s 37AH(1).[71] In short, therefore, the common law doctrine of tainting is not affected by or amenable to relief under the Illegal Contracts Act but, in present circumstances, it is amenable to relief under the relevant provisions of the Securities Act.

Tainting – criteria

[136] The next step is to examine the criteria for the application of the doctrine of tainting in greater detail. A helpful case on the subject is *In re Trepca Mines Ltd (No 2),* a decision of the Court of Appeal in England comprising Lord Denning MR and Donovan and Pearson LJJ.[72] In that case a solicitor was held to be disentitled to

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71 I say that without prejudice to whether any such relief would be appropriate.
72 *In re Trepca Mines Ltd (No 2)* [1963] Ch 199 (CA).

costs because he was actively implicated in a champertous agreement between his client and a funder of the client's litigation who had contracted to receive 25 per cent of the proceeds of the claim if it was successful.

[137] The champertous agreement between the solicitor's client and the funder was the primary contract. It was illegal. The collateral contract was the contract of retainer between the client and the solicitor. The collateral contract was held to be sufficiently tainted by the illegal primary contract so as to disentitle the solicitor from enforcing his bill of costs. Lord Denning said that, even though the solicitor was not a party to the champertous contract:[73]

> ... if he is an active participator in this sense, that he voluntarily does a positive act to assist to implement the unlawful agreement, then he cannot recover; for, by rendering positive assistance, he becomes guilty of aiding and abetting the offence and is himself guilty of it.

[138] When expressing his conclusion, Lord Denning said that the solicitor had actively participated in the champertous arrangement. That arrangement was unlawful and accordingly the solicitor's bill of costs was tainted with champerty and he could not recover.

[139] Donovan LJ said that the solicitor had "aided and abetted" the champerty and the court would not lend its aid to him when he sought to recover his costs.[74] Pearson LJ reviewed the case law in some detail[75] and, in the course of doing so, cited from the judgments of the English Court of Appeal in *Scott v Brown Doering McNab & Co*.[76] In that case Lindley LJ had said that the Court would not lend its aid to anyone who was "implicated" in any relevant illegality.[77]

[140] The references to aiding and abetting in *Trepca Mines* lead one naturally to consider the concept of party liability in relation to offences. Champerty was an offence in England at the time and in the present case issuing securities to the public in contravention of the Securities Act can similarly amount to an offence if the necessary criteria are established. If that is so, an offence under s 59 of the

73 At 221.
74 At 223–224.
75 At 228.
76 *Scott v Brown, Doering, McNab & Co* [1892] 2 QB 724 (CA).
77 At 728.

Securities Act is committed, among others, by any issuer or promoter of the securities. However, in the case of a promoter, but not an issuer, it is a defence to show that the contravention did not take place with the promoter's knowledge and consent.

[141] Section 66 of the Crimes Act 1961 provides that everyone is party to and guilty of an offence who (a) actually commits the offence; or (b) does or omits an act for the purpose of aiding any person to commit the offence; or (c) abets any person in the commission of the offence. An offence for this purpose means any act or omission for which anyone can be punished under the Crimes Act or under any other enactment, whether on conviction on indictment or on summary conviction.[78] It follows that if the developers aided and abetted Blue Chip in the invalid and unlawful issue of the debt securities, they also committed an offence under s 59 and, as an issuer, they cannot claim the benefit of the defence created by s 59(2)(b).

[142] My purpose in referring to the criminal analogue has been to indicate that in a case like the present there is likely to be a substantial overlap between the common law doctrine of tainting and the criminal law concepts which render people guilty as parties to an offence pursuant to s 66 of the Crimes Act. I will examine later whether the purposes and policies attendant on secondary liability in crime and those that apply to the doctrine of tainting should be the same.

Application of tainting doctrine

[143] I return to what must be shown to establish that the sale and purchase agreements were unenforceable as a result of being tainted by their association with the primary contract between the investors and Blue Chip. In this respect I see no material difference between the three Blue Chip products. They were each in substance a means of financing the investors into the apartments and indeed a means whereby the investors funded Blue Chip's interest in the apartments.

[144] The collateral contract in this case involves a third party, that is, someone who is not a party to the primary contract. It is necessary as a first step to consider

[78] See definition of offence in s 2(1) of the Crimes Act 1961.

whether the collateral contract is sufficiently related to the primary contract so that it can fairly be said that the unenforceability of the primary contract should lead to the unenforceability of the collateral contract. That will be so if, for example, the collateral contract is a necessary part of a composite arrangement of which the primary contract is also a part. In such circumstances the collateral contract assists the implementation of the primary contract.

[145] There can be no doubt that this criterion is satisfied in the present case. Here the collateral and primary contracts were interdependent. If an analogy were made with the concept of severance there could be no question of the collateral contract being severed from the primary contract. The primary contract represented, in substance, the means by which the investors were to finance, and thereby implement, the collateral sale and purchase contract. The linkage between the two is immediate and self-evident. The second question that arises is what, if any, knowledge the third party must have to render the collateral contract unenforceable by reason of its being tainted by the illegality of the primary contract.

Knowledge

[146] One of the few reasonably recent cases on this subject is the decision of our Court of Appeal in *Portland Holdings Ltd v Cameo Motors Ltd*.[79] For present purposes it is sufficient to say that there are passages in the judgments which suggest that it is not necessary that a third party have actual knowledge of the relevant matters and that constructive knowledge (ought to have known) is sufficient. Before returning to that issue and considering *Portland* in more detail, I will consider whether as a matter of policy, in the present context at least, the third party need have any knowledge of the illegality of the primary contract. I am referring here to knowledge of the facts and circumstances which give rise to the illegality, rather than knowledge that those facts and circumstances result in there being illegality. For reasons to which I will come, I am of the view that, if knowledge is necessary at all, knowledge of the facts and circumstances is sufficient without there having to be any knowledge that those facts and circumstances give rise to illegality.

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79 *Portland Holdings Ltd v Cameo Motors Ltd* [1966] NZLR 571 (CA).

[147] One of the purposes of s 37 of the Securities Act is to prevent a party who contravenes the section from receiving any benefit from the contravening transaction. As we have seen, if a benefit has been received it must be restored. The offending party suffers the consequences of s 37, whatever their state of mind might have been. It is enough that they have conducted themselves in such a way as to contravene the section, whether they are aware of doing so or not. I consider the same position should apply to a third party who, by means of a sufficiently related collateral contract, also gains a benefit from the contravening conduct.[80] The purpose and policy of the Act applies equally to a person in that situation. If the contracts are sufficiently interwoven, and the third party thereby stands to benefit from the contravening transaction, that party should suffer the same consequences as the party who benefits from the primary contract. On this basis I would hold that the collateral sale and purchase contracts entered into between the developers and the investors were tainted by the primary contracts. They are therefore unenforceable.

[148] This conclusion is supported by the author of Treitel who states that, in general, ignorance of the law or a mistake of law does not give a party the right to enforce a contract which is "affected" by illegality.[81] The reference to the contract being affected by illegality is directed to the primary contract, but it can appropriately also apply to a collateral contract that is sufficiently related to the primary contract. The proposition applies also to ignorance of matters of fact as well as matters of law. Treitel discusses cases where a party to an illegal contract does not know of the facts making the contract illegal. The right of such a party to enforce the contract has been upheld in some cases but denied in others. Various ways of deciding on which side of the line a particular case falls are then considered. The author suggests, and I agree, that in the case of statutory illegality, as here, the answer should turn on the purpose and policy of the statute.

[149] In the present case, the statutory purpose is to protect vulnerable members of the investing public. That purpose would not be well served if a party to a collateral contract otherwise caught by the doctrine of tainting, could avoid the consequences

80 None of cases referred to in the books has had to confront the question whether knowledge is required in a case such as the present.
81 At [11-116].

by demonstrating ignorance of a relevant matter of fact or law. In *Archbolds (Freightage) Ltd v S Spanglett Ltd*[82] Devlin LJ regarded the question as being whether the purpose of the statute would be sufficiently served by permitting enforceability where there was lack of knowledge.[83] In the present context I do not consider the statutory purpose would be sufficiently served by that approach. I say that as a matter of general principle and without prejudice to what weight lack of knowledge should have in any particular case when the court is considering an application for a relief order.

Constructive knowledge

[150] Despite the conclusion just expressed, I will go on to consider what form of knowledge should be required of the third party if one were to take the view that some form of knowledge is necessary. Wilful blindness can be equated with actual knowledge. So the question to be addressed comes down to whether it should be sufficient for tainting, in present circumstances, that the third party has constructive knowledge of, that is, ought to have known of, the facts and circumstances which give rise to the illegality of the primary contract.

[151] The concept of constructive knowledge was first employed by the courts of equity primarily to deal with cases where one party was vulnerable to influence from or liable to be taken advantage of by another, often stronger, person. The vulnerability usually arose out of the relationship between the parties but could also arise from some ad hoc situational circumstance. The approach of equity was that the stronger party could not in good conscience be allowed to excuse themselves by claiming a lack of actual knowledge, when in the circumstances they ought to have known of the facts or circumstances in issue. If a party ought to have had that knowledge, equity would not allow them to benefit from lack of actual knowledge. In part this was due to the difficulties that can attend proof of actual knowledge; but equity also took this approach to strike a fairer balance between the vulnerable and those with whom they dealt. It was, of course, one of the primary roles of the Courts

82 *Archbolds (Freightage) Ltd v S Spanglett Ltd* [1961] 1 QB 374 (CA).
83 At 390.

of Chancery to protect the vulnerable from unconscionable dealings which the common law courts were less able to control.

[152] Section 37 of the Securities Act is designed to protect investors when offers of securities are made to the public.[84] The Act is designed to ameliorate that vulnerability. It is appropriate to bring that purpose to bear on the question whether constructive knowledge should suffice in the circumstances we are addressing. In my view it would not be consistent with the purpose of the Act to allow someone who did not actually know, but should have known of, the relevant facts to escape the consequences of being sufficiently implicated in a tainted transaction.

[153] I should add that the reasoning I have set out in support of the proposition that constructive knowledge should suffice, also supports my primary and preferred view that no knowledge should be required by the third party in cases where that party will benefit via the collateral contract from the illegal primary contract. The purposes and policy of the Securities Act are such that a sufficient linkage between the contracts, coupled with the fact that the third party derives a benefit from the illegality, should be enough to render the collateral contract unenforceable by the third party.

If relevant, knowledge of what?

[154] I return to a point I deferred earlier and address it on the premise that, contrary to my preferred view, some kind of knowledge is required of the third party. When one is speaking of the knowledge of a person who assists another to do something unlawful, what is it that the assistant (secondary) party must know? Is it the facts which give rise to the unlawfulness or is it, in addition, that those facts constitute unlawful conduct? The general rule in crime is that, in order to be guilty of aiding and abetting, the secondary party must have knowledge of the essential matters of fact that constitute the offence and must intend to help the primary party

[84] See *Re AIC Merchant Finances Ltd* [1990] 2 NZLR 385 (CA) at 394.

to perform the acts involved. It is not necessary as an essential matter for the secondary party to know that the relevant acts amount to an offence.[85] For example, a secondary party to murder does not have to know that an intentional killing by the principal party amounts in law to murder. All the secondary party needs to know is that the principal party intends to kill.

[155] That being the case in crime, the question is whether the position should be different in tainting cases. This question comes down to whether the third party in a case of alleged tainting must know that the primary contract involves illegality. Or is it sufficient that the third party is aware simply of the essential facts which give rise to the illegality of the primary contract?

[156] The policy behind the doctrine of tainting is relevant to this inquiry. Essentially, it is that a party to a collateral contract cannot enforce that contract when to do so would either, directly or indirectly, allow that party to benefit from an illegality in which he is sufficiently implicated. Parties to the primary contract cannot enforce it at common law, irrespective of whether, at the time of contracting, they knew that illegality was involved. Should the position be different in the case of a party to a collateral contract?

[157] I cannot discern any basis for departing in tainting cases from the general rule that applies to criminal complicity. In both the civil and criminal contexts the requirement should be knowledge of the essential matters that give rise to the illegality but not knowledge of the illegality itself. A person will not be implicated in the illegality of the principal contract unless the collateral contract is sufficiently related to the primary contract. If that is shown, and the party to the collateral contract knew or ought to have known of the essential facts giving rise to the illegality, I consider this form of knowledge should be sufficient for the doctrine of tainting to apply without there being any need for knowledge of the legal consequences of the essential matters.

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85 See Bruce Robertson (ed) *Adams on Criminal Law* (looseleaf ed, Thomson Reuters) at [CA 66.19(1)]; and David Ormerod *Smith and Hogan's Criminal Law* (13th ed, Oxford University Press, London, 2011) at [8.4.2.2]; and the cases cited in both works.

[158] As I have shown earlier, the doctrine of tainting is closely related conceptually to party liability in the criminal context. It would be anomalous if, for the purpose of party liability, no knowledge of the illegality was required, but such knowledge was required for tainting purposes. But, of course, as I have already emphasised, my preferred view is that it is not necessary that the third party have any knowledge of the facts and circumstances giving rise to the illegality of the primary contract. Gaining a benefit through sufficient factual complicity should suffice.

***Portland Holdings* case**

[159] My views on tainting do not coincide with those of the Court of Appeal in the present case. That Court placed some reliance on the decision in *Portland Holdings*. I must therefore consider that case further. The first thing to notice is that there is a material difference between the facts of that case and this. *Portland Holdings* involved an invalid and illegal hire purchase agreement between a car dealer (Cameo) and a customer. The agreement was later assigned to a financier (Portland). The assignment did not in any way assist the implementation of the earlier hire purchase agreement which had already been independently entered into. It simply transferred the benefit of the agreement from the dealer to the financier. The primary contract of hire purchase and the collateral contract of assignment were not interdependent. As North P said, the assignment was a "separate and later transaction".[86]

[160] It was essentially for these reasons that in *Portland Holdings* the Court of Appeal decided there was no tainting. Their Honours' discussion about knowledge must been seen in that light. It was accepted by all concerned that the financier as assignee could not enforce the invalid hire purchase agreement against the original debtor, the customer. What the Court of Appeal held was that the financier could enforce the dealer's covenants in the assignment. The facts of the present case are well removed from that situation. The nub of *Portland Holdings* seems to me to lie in the judgment of Turner J where his Honour said: [87]

86 At 583.
87 At 581.

> As regards contracts, not between the two original parties to an illegal contract, but between one of them and a third party, the policy of the law appears to me to render unenforceable by the taint of illegality those contracts, ex facie legal, the purpose and object of which is to secure *in the future* some illegal or immoral end. The principle appears to me well expressed in *8 Halsbury's Laws of England*, 3rd ed. 128 where it is stated:
>
>> An agreement which is innocent in form cannot be enforced if it is entered into for the purpose of carrying out or assisting in carrying out an illegal transaction.
>
> In the present case I am unable to see what future illegal end was purposed by the covenants in the assignment. The illegality which is said to taint the assignment is (considering the matter at the date of execution of the assignment) already in the past. There is, as at the date of execution of the assignment, already in existence a contract void for non-compliance with the regulations. The assignment of such a contract is not itself illegal; it is prohibited by no statute. Nor does such an assignment encourage or enable any illegal act to be done which is not yet done.

[161] In the present case the collateral contract undoubtedly assisted in carrying out the illegal transaction embodied in the primary contract. I do not consider *Portland Holdings* precludes the conclusion that in a case like the present the doctrine of tainting should apply and that the state of mind of the third party should not be a relevant consideration. But, if knowledge were to be a necessary element in a tainting case such as the present, the reasoning in *Portland Holdings* does not suggest with any persuasive force that constructive knowledge is insufficient. McCarthy J expressly accepted that constructive knowledge would be enough.[88] Neither Turner J nor North P said it should not and, for the reasons already given, I agree with McCarthy J.

Conclusion

[162] In the light of my conclusions I agree that the appeals should be allowed with the consequences proposed by William Young J.

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88 At 597.