#114

IN THE COURT OF APPEAL OF NEW ZEALAND

CA157/2010
[2010] NZCA 425

	BETWEEN	BROWNS REAL ESTATE LIMITED Appellant
	AND	GRAND LAKES PROPERTIES LIMITED Respondent

Hearing: 19 August 2010

Court: Glazebrook, Venning and Simon France JJ

Counsel: P R W Chisnall for Appellant
D M Lester for Respondent

Judgment: 20 September 2010 at 4.30 pm

JUDGMENT OF THE COURT

A The appeal is dismissed.

B Costs for a standard appeal on a band A basis plus usual disbursements are awarded to the respondent.

REASONS OF THE COURT

(Given by Glazebrook J)

Introduction

[1] On 27 November 2009 Grand Lakes Properties Ltd (Grand Lakes) served a statutory demand on Browns Real Estate Ltd (Browns) for the sum of $134,931.00. The demand is for money owing pursuant to a lease of retail units in Queenstown.

[2] On 10 March 2010 Associate Judge Osborne refused Browns' application, under s 290(4)(b) of the Companies Act 1993, to set aside the statutory demand.[1] Browns appeals against that decision.

Relevant legislation

[3] The relevant legislation is s 290(4) of the Companies Act. It provides:

> (4) The Court may grant an application to set aside a statutory demand if it is satisfied that:
>
> (a) There is a substantial dispute whether or not the debt is owing or is due; or
>
> (b) The company appears to have a counterclaim, set-off, or cross-demand and the amount specified in the demand less the amount of the counterclaim, set-off, or cross-demand is less than the prescribed amount; or
>
> (c) The demand ought to be set aside on other grounds.

Judgment of Associate Judge Osborne

[4] In the High Court, Browns sought to set aside the statutory demand under s 290(4)(b) on the basis that it had a counterclaim which exceeded the sum demanded. The counterclaim arose from alleged misrepresentations about the quality and characteristics of the retail precinct made by the lessor (Grand Lakes' predecessor in title) or its agent during discussions and negotiations regarding the lease that occurred throughout 2006. Associate Judge Osborne accepted that Browns had an arguable case that Grand Lakes' predecessor in title as lessor misrepresented the qualities and characteristics of the retail precinct. The Associate Judge also accepted that the misrepresentation arguably resulted in damage to Browns in excess of the statutory demand amount.

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[1] *Browns Real Estate Ltd v Grand Lakes Properties Ltd* HC Invercargill CIV-2009-425-670, 10 March 2010.

[5] However, the Associate Judge held that cl 3.1 of the lease precluded Browns from raising a set-off, counterclaim or cross-demand as an excuse for not paying rent. Clause 3.1 of the lease (the no set-off clause) provides:

> **Payment**: The Lessee shall in each year during the Term, pay the Rent and any other money required to be paid by the Lessee pursuant to this Lease, to the Lessor without demand from the Lessor and free of any deduction, withholding, set-off or reduction on any account.

[6] The Associate Judge was of the view that cl 3.1 could be described as a traditional no set-off clause, designed to deal with the finding of the Court of Appeal in *Grant v NZMC Ltd* that the words "free and clear of exchange or any deduction whatsoever" did not preclude the right to equitable set-off in the summary judgment context.[2] With regard to the issue as to whether Browns was precluded from pursuing any counterclaim or cross-demand pursuant to cl 3.1, the Associate Judge noted that this would depend on the correct construction of the contract and the obligations the parties agreed to.

[7] The Associate Judge held that Browns had no arguable case on the wording of the contract to raise a set-off or counterclaim as an excuse for not paying rent. Therefore, it was held that Browns had to pay the rent and then separately pursue any available remedies elsewhere with such other mechanisms as would remain available to it.

[8] The Associate Judge also came to the preliminary view that the arbitration and two-year time bar provisions of cl 20 of the lease[3] precluded the cross-demand or counterclaim asserted by Browns. He also rejected the submission that there had been any representation or estoppel arising out of the negotiations with Grand Lakes' predecessors in title, including by the receivers of the immediate predecessor in title. These were negotiations arising out of the alleged misrepresentation about the quality of the retail precinct which resulted in reduced rent being paid on a without prejudice basis. Finally, Associate Judge Osborne rejected as a ground of opposition that Browns was solvent as it had filed no proper evidence to support this contention.

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2 *Grant v NZMC Ltd* [1989] 1 NZLR 8 (CA) at 13.

3 Clause 20 of the lease required any disputes under the lease to be submitted to arbitration within two years of the time when the matter or matters giving rise to the dispute first came to the attention of the party seeking to commence the arbitral proceedings.

Browns' submissions

[9] Browns submits that Associate Judge Osborne was wrong to conclude that cl 3.1 of the lease precludes Browns from raising an arguable counterclaim in relation to the statutory demand. In its submission, the correct position with regard to setting aside a statutory demand on the basis of an existing counterclaim was set out in *Pacific Forum Ltd v New Bay Holdings Ltd.*[4] In *Pacific Forum*, it was held that a clause providing that rent should be paid "without demand from the lessor and without any deduction" could not override the Court's power to set aside the statutory demand under s 290(4)(b) when the applicant appeared to have a counterclaim.[5]

[10] Browns claims that, if the parties had wanted to exclude the ability for Browns to apply to the Court under s 290(4)(b) to have the statutory demand set aside, then a specific clause would have been needed. Browns emphasises that there is no need for any link between the amount claimed in the statutory demand and the subject matter of the cross-claim or counterclaim relied upon.[6]

[11] On the other points made in the Associate Judge's judgment, Browns submits that there is an arguable case that the limitation in the arbitration clause was waived by the correspondence with the receivers.

Grand Lakes' submissions

[12] Grand Lakes submits that cl 3.1 of the lease prevents a debtor relying on s 290(4)(b) as it is sufficiently wide to prohibit a set-off, counterclaim or other deduction. It is accepted that the clause does not prevent Browns raising other grounds under s 290(4)(c). As a backup argument, Grand Lakes argues that the Court's discretion should always be exercised in favour of the creditor and the statutory demand not set aside where there is a contractual no set-off provision. Grand Lakes points out that this Court has said in the summary judgment context that, in circumstances where set-off is excluded by an express contractual provision

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4 *Pacific Forum Line Ltd v New Bay Holdings Ltd* HC Auckland M141/96, 4 April 1996.

5 At 9.

6 *Phoenix Organics Ltd v RD2 International Ltd* (2003) 9 NZCLC 263,380 (HC). In this case of course there is a link.

in an agreement between commercial parties, there is no injustice in giving effect to the bargain the parties have made.[7]

[13] As to the other issues, Grand Lakes says that the limitation provision in cl 20 of the lease clearly applies to Browns' counterclaim. It is submitted further that a company that is contractually prevented from raising a set-off, counterclaim or cross-demand in respect of an unpaid debt must be seen as insolvent if it cannot otherwise meet that debt than through the cross-demand, counterclaim or set-off.

Discussion

[14] In our view, by raising the counterclaim in response to the statutory demand, Browns is seeking to justify the non-payment of the rent. In so doing, Browns are in breach of cl 3.1 which prohibits withholding of rent (and any other payments due under the lease) on any account. Associate Judge Osborne was correct to conclude that the clause at issue in this case precludes this.

[15] We now move to a consideration of Grand Lakes' submission that a contractual no set-off provision of the type at issue in this case precludes a party making a successful application to set aside a statutory demand under s 290(4)(b). In *Laywood v Holmes Construction Wellington Limited*, this Court, in the context of the Construction Contracts Act 2002 (CCA), reasoned that because s 79 of the CCA precludes a court, except in limited circumstances, from giving effect to a counterclaim, set-off or cross-demand when a sum is payable under the CCA, a debtor would therefore be prevented from relying on the existence of a counterclaim, set-off or cross-demand in any application to set aside a statutory demand.[8] The *Laywood* reasoning was driven by the view that to give effect to a counterclaim, set-off, or cross-demand would recreate the problems that led to the enactment of the CCA and frustrate the underlying purpose of the statute.[9] As noted in *Laywood*,

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7 *Bromley Industries Limited v Martin and Judith Fitzsimons Limited* [2009] NZCA 382 at [66].

8 *Laywood v Holmes Construction Wellington Limited* [2009] NZCA 35, [2009] 2 NZLR 243 at [61]–[65]. This case concerned a bankruptcy notice and so the remarks on statutory demands were strictly obiter but Browns did not suggest any reason for distinguishing between bankruptcy notices and statutory demands in this context.

9 At [63]–[64].

statutory demands and bankruptcy notices are, in a practical sense, important debt enforcement mechanisms.[10]

[16] While it is true that the Court in *Laywood* was dealing with effectively a clash between two statutes, similar reasoning applies where there is a contractual no set-off provision. Just as in the CCA context, the efficacy of a no set-off contractual provision would be undermined if statutory demands could be set aside on the basis of a set-off, counterclaim or cross-demand a commercial party had by contract expressly agreed could not be raised. In such a situation, there seems no reason in principle why statutory demands and bankruptcy notices should not be available as debt enforcement measures when, as was conceded by Browns, other enforcement measures would be (including summary judgment). Further, we accept Grand Lakes' submission that an inability to meet the statutory demand, without recourse to the set-off or counterclaim which it is prevented from raising, would mean that Browns is insolvent: ie it would be unable to pay its debts as they become due in the normal course of business.[11]

[17] We do not accept Browns' submission that a specific reference excluding the statutory demand procedure is needed. There is a question as to whether a contractual provision, however worded, can totally oust the jurisdiction of the courts to consider a counterclaim, set-off or cross-demand. However, this is an issue that is more theoretical than real. In our view a contractual no set-off provision of the type at issue in this case would normally result in the court's discretion being exercised against an applicant if the sole grounds for an application to set aside a statutory demand was the existence of a set-off, counterclaim or cross-demand which a party had expressly agreed could not be raised. We consider that commercial parties should be required to honour the bargain they have made,[12] absent other grounds that tell against the recognition of a statutory demand. Grand Lakes, rightly in our view,

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10 At [62].

11 See the solvency test that is set out in s 4(1) of the Companies Act.

12 Just as in the summary judgment context: see at [12] above. We are cognisant of comments by this Court that it will only be in rare cases that statutory demands will not be set aside where the necessary jurisdiction has been established under s 290(4)(a) or (b): see eg *Primary Health Remuera Ltd v Avoca Residential Construction Ltd* (2004) 9 NZCLC 263, 647 (CA) at [42] and *Alfex Doors & Windows Ltd v Alutech Windows and Doors* (2001) 16 PRNZ 963. However, those comments were not made in the context of cases where there was a contractual no set-off clause.

conceded that an application to set aside the demand can be made under s 290(4)(c).[13] Such an application would, however, need to be on grounds other than the existence of a set-off or counterclaim.[14]

[18] As to the other matters, we consider that there are strong grounds for considering that the claim by Browns is barred by cl 20 of the lease although, like Associate Judge Osborne, we make no definitive finding on that point. We also make no definitive finding on the submission that there had been a waiver of the requirements of cl 20 but it appears unlikely in the context of the correspondence relied upon.

Result

[19] The appeal is dismissed.

[20] Costs for a standard appeal on a band A basis plus usual disbursements are awarded to the respondent.

Solicitors:
Gibson Sheat, Lower Hutt for Appellant
Layburn Hodgins, Christchurch for Respondent

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13 For a discussion of the other grounds that have been considered to warrant setting aside a statutory demand, see generally, *Commissioner of Inland Revenue v Chester Trustee Services* [2003] 1 NZLR 395 (CA).

14 It may be that a court would consider the existence of a counterclaim, set off or cross-demand if there are also other grounds relied on for setting aside a statutory demand. We leave that question open.