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**IN THE HIGH COURT OF NEW ZEALAND
BLLENHEIM REGISTRY**

CIV 2008 406 108

BETWEEN MICHELE SAINT-ALEXIS AND
PATRICK ERGAS
Appellants

AND JAMES ADAIR HANNA
Respondent

Hearing: 17 June 2008
(Heard at Wellington)

Counsel: M Hardy-Jones for appellants
F Donaldson for respondent

Judgment: 24 June 2008

RESERVED JUDGMENT OF DOBSON J

[1] The appellants in this appeal were sued in the Blenheim District Court, in their capacity as the trustees of the Te Ruahine Trust, for failure to pay a payment claim issued to them under the provisions of the Construction Contracts Act 2002 (“the Act”) by the respondent, who purported to sue in his capacity as the trustee of the East West Pacific Trust (“EWPT”). The respondent (“Mr Hanna”) is an architect, and the claim related to work done on a property owned by the Te Ruahine Trust.

[2] The appeal is brought from a grant of summary judgment ordered in District Court Judge Zohrab’s reserved decision, delivered on 16 April 2008. The judgment carefully traversed a range of issues, the majority of which are not in issue on the appeal. These included the inclusion in the payment claim of categories of work not covered by the Act, which Mr Hanna abandoned. The Court permitted amendment

to reduce the claim by the relevant amount down to \$28,395.06 plus GST. A further issue was that the attempted reply to the claim by the appellants did not qualify as a payment schedule under s 21 of the Act so as to afford a ground for resisting the contractor's entitlement to prompt payment.

[3] The Act is recognised as effecting a material change in favour of contractors and sub-contractors when disputes arise in the construction industry. Judicial observations in cases applying the Act reflect the importance of “cash flow in the building trade as the very life blood of the enterprise” (per the Court of Appeal in *George Developments Ltd v Canan Construction Ltd* [2006] 1 NZLR 177) and that:

Should the principal not follow the correct procedure it can be obliged to pay in the interim what is claimed, whatever the merits. In that way if the principal does not act in accordance with the quick procedures of the Act, that principal, rather than the contractor and sub contractors, will have to bear the consequences of delay in terms of cash flow. (per Asher J in *Marsden Villas Ltd v Wooding Construction Ltd* HC Auckland CIV 2006 404 2136 25 May 2006)

[4] That position under the Act was not challenged at all on appeal. Rather, the appellants challenged Mr Hanna's standing to sue as trustee for the EWPT. Although on its face this was a technical point to take, they argue that the context makes it a substantive point. The appellants commenced their own District Court proceedings against Mr Hanna, for overpayment and breach of contract, some months before Mr Hanna commenced his summary judgment proceedings in reliance on the payment claim under the Act. The appellants characterise his proceedings as a pre-emptive strike, intended to use the Act to force prompt payment before the appellants can get their proceedings, inevitably pursued on a conventional basis, to a substantive hearing. That tactic would be entirely legitimate if Mr Hanna has nominated the correct entity as claimant. The mis-match between the trust he sues for, and himself as the defendant to the appellants' earlier claims may, however, frustrate a resolution of the overall dispute.

[5] That justifies the appellants focusing on the identity of the claimant against them with some care. The two arguments for the appellants relating to the status of the entity with whom their trust dealt were:

- a) First, that there was no trustee of the EWPT, because the terms of its deed exclude the prospect of another trust being a trustee. Shortly before the summary judgment hearing, Mr Hanna had clarified that a second trust, the Churchill Foundation Trust (“CFT”), was in fact the trustee of the EWPT, with him suing in his capacity as trustee of the CFT. If the CFT could not be a trustee, then EWPT was not lawfully constituted, and would lack capacity to sue.

- b) Secondly, even if another trust could be appointed as trustee of the EWPT, then the evidence as to how the appointment of the CFT was supposed to have occurred raised questions, arguably sufficient to cast doubt on Mr Hanna’s evidence on the point, so that a credibility issue arose on which the Court should permit cross-examination at a substantive hearing.

[6] The first question is a matter of interpretation of the trust deed providing for formation of the EWPT. Clause 6.1 of that trust provided:

The trustee shall at all times be a Person, Constitutional Corporation or Association and may be a member of the trust.

(Although capitalised, those three terms are not defined in the trust deed.)

The terms used for formation of both trusts in issue were in identical terms, and I was advised that they follow a standard form for trusts used in Australia for tax minimisation purposes.

[7] The first possible interpretation of the permissible scope of trustees in clause 6.1 is that any person, constitutional corporation or association qualifies for appointment as trustee, and that in addition others not coming within those categories may also be appointed if they are a member of the trust. Under clause 5.1 of the trust deed, membership of the trust extended to natural persons, trusts and registered companies that had been duly nominated and approved. Mr Hanna’s evidence was that the CFT had been made a member of the EWPT. It was therefore

qualified to act as trustee of the EWPT. This interpretation was upheld by the District Court.

[8] However, a second interpretation of clause 6.1, which was argued for the appellants, was that the last phrase "...and may be a member of the trust" did not expand the categories of potential trustee, but merely confirmed that any person, constitutional corporation or association was not disqualified from acting as trustee by virtue of also being a member of the trust. There is a practical rationale for such a clarification. Where a trustee's powers extend to discretionary considerations as between different members/beneficiaries, status as a member/beneficiary raises the prospect of a conflict between duty and interest. A settlor would accordingly be likely to address, when forming the trust, whether members could also participate in directing the affairs of the trust as a trustee.

[9] I consider the juxtaposition of "shall" and "may" in the terms of clause 6.1, and the context of that provision in the trust deed, strongly supports this second interpretation. "Shall" connotes a mandatory requirement that any trustee be a person, constitutional corporation, or association. That requirement would not be complied with if a member, who was not one of those three things, was appointed as trustee.

[10] Mr Hardy-Jones also argued for the appellants that there is no scope in law for one trust to be appointed as trustee of another trust because the trustees of the first trust will be constrained to act in the interests of the beneficiaries of that first trust. Accordingly, the prospect of being unable to act in the sole interests of the second trust would, as a matter of principle, disqualify the first trust from accepting appointment. Mr Hardy-Jones further foreshadowed more wide-ranging attacks on the lawfulness of the EWPT, citing the absence of any provision for a perpetuities period to apply as an example of the respects in which the trust deed did not conform with the requirements for a lawful trust under New Zealand law.

[11] These further arguments would depend on acceptance of the proposition that the trust had to be validly constituted in terms of New Zealand law, before it could be recognised for the purposes of contracting in this country. That is an issue about

which, on the view I have come to, it is unnecessary to reach a view for present purposes. The only basis on which Mr Hanna claimed was that the EWPT had contracted with the Te Ruahine Trust and had followed the procedure under the Act which now entitled it to be paid. If, when challenged, a fundamental flaw is revealed about the lawful existence of the trust which must be a pre-condition to its ability to enter contracts and to sue, then that must raise, at the very least, an arguable defence, and that is all the appellants need to do in the present context.

[12] Mr Donaldson urged me to adopt a common sense approach, as the learned District Court Judge described himself as doing: the appellants had, until the dispute arose, been content to deal with the EWPT, their cheques had been payable to that trust, and its standing was sufficient to be a GST registered entity. However, Mr Hardy-Jones responded that payment of cheques, at Mr Hanna's direction, to any third party does not amount to an acknowledgement by the appellants that they had contracted with any such third party. Now that a dispute had arisen, it was important to resolve the identity of those liable on each side. Where, as here, the appellants had commenced proceedings first against Mr Hanna in his personal capacity, it was important to ensure that the correct parties with capacity to sue and be sued were committed to all aspects of the dispute. I accept the essence of these points.

[13] As to the status of EWPT as a GST registered entity, such registration proceeds because Inland Revenue is required to capture GST by all traders. Registration cannot be treated as any warranty of the lawful creation of the registered taxpayer, or that the lawful constitution of a GST registered entity has been vetted by the Department.

[14] Although it was not argued in these terms by Mr Donaldson, it would be consistent with the learned Judge's resort to common sense to ask what difference it makes, whether the trust on whose behalf Mr Hanna sued was properly constituted or not. The trust has no status as a separate legal entity and could only act by its trustee or trustees, the trustee would be personally liable for costs in favour of a successful defendant (subject to his right of reimbursement from the trust) and the presence or absence of a trust in the contractual chain between Mr Hanna and the principal requesting the work had not affected the way the work was performed. The

difficulty with that approach is that it ignores the need for certainty as to the identity of contracting parties, certainly once claims and counterclaims are raised. The Te Ruahine trustees have sued Mr Hanna. If he wrongly thought that he could interpose a particular trust (entirely for his own purposes and not affecting the provision of works and services that the principal was to receive), but he is mistaken in that regard, then he has contracted in his personal capacity and can only sue and be sued in that form.

[15] The appellants' second argument was to the effect that if they were wrong as to the absence of legal capacity to create the trust, then the factual circumstances in which it was claimed to occur nonetheless gave rise to sufficient grounds for questioning the explanation provided, to raise credibility issues requiring cross-examination before they could be resolved. It would follow that an arguable defence to the plaintiff's asserted capacity to contract, and to sue for breach of that contract, was established, requiring a substantive hearing.

[16] Both trust deeds for EWPT and the CFT purport to have been concluded on 6 April 2004, at which time Mr Hanna was an undischarged bankrupt in Australia. Mr Hardy-Jones postulated that the CFT had to be completed first for there to be a trustee in existence when the EWPT was formed. He relied on the witness to execution of the CFT deed specifying her residence in Blenheim as necessitating Mr Hanna completing the CFT deed in Blenheim, then flying to Sydney and completing the EWPT deed there on the same day. This all when his ability to leave Australia ought to have been constrained by those supervising his bankruptcy. In addition, Mr Hardy-Jones advised that only shortly before the District Court summary judgment hearing was a copy of the CFT deed produced, with no explanation for the failure to produce it earlier, and after the then solicitors for Mr Hanna had stated unequivocally that there were no further discoverable documents. Further, Mr Hardy-Jones suggested that the two deeds were precisely the same, down to certain typographical mistakes, and that there were issues to put to Mr Hanna in cross-examination as to the genuineness of the asserted timing of execution of the CFT deed.

[17] Mr Donaldson did not accept any basis for asserting an arguable defence on the circumstances of creation the two trusts. He urged that nothing had been raised which would justify any material doubt about Mr Hanna's sworn evidence going to the regularity of creation of the trusts, and that it was simply not an issue that raised any aspect of an arguable defence. The District Court Judge had treated the argument in that way.

[18] I would be inclined to treat the factual questions raised as adding somewhat to the weight of the prospective defences. If, however, my view on the first argument was wrong, and the legal capacity to appoint a trust as a trustee of EWPT was confirmed, then I doubt that these suspicions of irregularity would have been sufficient on their own to raise an arguable defence.

Conclusion

[19] I accordingly find that the learned District Court Judge erred in entering summary judgment, and that judgment is now set aside. Mr Hanna should have leave, at his option, to amend the capacity in which he pursues the claim. Although I am not in a position to make timetable orders for the future conduct of the proceedings, I urge the parties to seek a relatively early call of these proceedings and the earlier proceedings commenced by the appellants in the Blenheim District Court.

Dobson J

Solicitors:
Hardy-Jones Clark, Blenheim for appellants
Cousins & Associates, Christchurch for respondent