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Verano Properties Ltd v De Luen - (2010) 11 NZCPR 859

High Court Auckland
CIV-2009-404-7878

14, 26 April 2010
Hugh Williams J

Sale of land -- Specific performance -- Defence of impossibility -- Whether hardship at time of contract or exceptional circumstances since that time.

The defendants jointly and severally agreed to buy two lots in a subdivision developed by the plaintiff. They defaulted on the purchases and the plaintiff sought specific performance. Both defendants raised the defence of impossibility; that it would be impossible for them to be able to comply with any order for specific performance.

Held (reserved decision granting the application against the second defendant and dismissing it against the first defendant)

1 In respect of the first defendant, exceptional circumstances had arisen since the date of the contract such that it would have amounted to hardship and injustice to grant the plaintiff's application for specific performance (see [51], [52], [54]).

2 The second defendant failed to demonstrate hardship at the date of the contract or exceptional circumstances which had arisen since that date such that that it would have been a hardship amounting to injustice to allow the plaintiff's claim against her (see [57], [59], [60]).

Cases mentioned in judgment

Baker v McLaughlin [1967] NZLR 405 (SC).

D'Arcy-Smith v Stace (2003) 4 NZ ConvC 193,771, (2003) 10 TCLR 788 (HC).

Keats v Wallis [1953] NZLR 563 (SC).

Nicholas v Ingram [1958] NZLR 972 (SC).

Application

This was an application by the plaintiff, Verano Properties Ltd, for specific performance against the first defendant, Shona de Luen, and the second defendant, Virginia Rose Jones.

G Blanchard for the plaintiff.

D Cowan for the defendants.

HUGH WILLIAMS J.

Introduction

[1] The plaintiff, Verano Properties Ltd, has sued the defendants, Ms de Luen and Ms Jones, on a contract dated 8 January 2007 pursuant to which they jointly and severally agreed to buy lots 4 and 7 of Verano's subdivision at Mangawhai known as "Vista Verano".

[2] This hearing dealt with Verano's application for specific performance of the contract. Both defendants raise the recognised defence to claims for specific performance of impossibility on their part to settle.

[3] The central question at this hearing was whether the defendants had made out the impossibility defence to which they claimed to be entitled.

Facts

[4] Vista Verano is a residential subdivision of approximately 90 lots at Mangawhai, north of Auckland.

[5] Ms de Luen and Ms Jones, under their trade name of "Aotea Enterprises or nominee" contracted to buy lots 4 and 7 for $190,000 and $185,000 respectively. They admitted in evidence they signed the contract on a speculative basis believing - contrary to history and the warnings of economists and others - that land always appreciates in value. It is now common ground the current sale price for lots in Vista Verano - if buyers can be found -- is substantially lower than the contract prices.

[6] A deposit of $10,000 was paid in respect of each lot and the contract was conditional on Verano obtaining consents by 31 July 2008 to enable it to deposit the scheme plan and the identifier to the lots being issued by 30 July 2010. Buyers were required to settle on settlement date. In default of settlement within five business days after the date of service of a settlement notice the contracts expressly preserved Verano's right to sue for specific performance or cancel the agreement and sue for damages.

[7] This contract became unconditional on 7 October 2009. Settlement by the purchasers of lots 4 and 7 was due on 14 October 2009 but the defendants failed to settle the purchase of either. A settlement notice was served on 20 October 2009 but still no settlements eventuated. These proceedings were issued on 27 November 2009 seeking specific performance or damages in the alternative.

Impossibility defence to specific performance

[8] The terms and conditions on which courts decline to order specific performance against defendants on the ground that it is impossible for the latter to comply with the order are well settled. The defence stems from the twin facts that specific performance is an equitable remedy and is thus discretionary with that discretion being exercised so as to achieve the greatest measure of fairness to both parties, plus the fact that courts in equity do not make orders which are an exercise in futility, that is to say, in cases such as these, orders compliance with which is impossible for defendants.

[9] Because of the theory - however vestigial - of the sanctity of contract,[1] the defence is, however, subject to a number of moderately stringent conditions. One of the better descriptions of the doctrine and its limitations appears in Spry, *The Principles of Equitable Remedies*,[2] where the following appears under the heading "Impossibility of Performance":

> A distinction must be drawn between cases where performance is impossible and cases where performance would be futile. On the one hand, questions of impossibility of performance arise where there is a prospect that it will not be within the power of the defendant to comply with the proposed order of the court. On the other hand, questions of futility of performance arise where there may not be a sufficiently high probability that the making of the proposed order will provide a sufficient benefit to the plaintiff to render that order just in all circumstances.
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> ...
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> It is clearly established that the courts will not require that to be done which cannot be done. ... But this is not to say that the mere anticipation of possible difficulties leads to a refusal of relief. If, on the materials before the court, performance may or may not be

> able to be completed, the various probabilities will be taken into account in deciding on the order that is most just in all the circumstances. Thus it may be most appropriate to order specific performance in the ordinary manner, so that if necessary the defendant may later approach the court for a modification or variation by reason of subsequent difficulties or may rely upon them in any subsequent proceedings in relation to the enforcement of the order. Again, if at the time of the original application there is shown to be a substantial risk that performance will not be possible, it may be most appropriate to make a conditional order or else to adjourn the proceedings until the position becomes more clear. Finally, if a sufficiently great likelihood is shown that performance will not be possible, and especially if no strong considerations of hardship appear on the part of the plaintiff, it may be most just to make no order for specific performance at all, whether absolute or conditional, and so to confine the plaintiff to remedies in damages.

[10] Some of the limitations on the doctrine are stressed by the learned authors of McGhee et al *Snells Equity*[3] where the following appears:

> The fact that one party has made a poor bargain, or that he is financially unable to complete, is not hardship, nor is inadequacy of price a ground for refusing specific performance, unless the purchaser stands in a fiduciary position to the vendor, or fraud enters into the contract. The reason is that, save in exceptional circumstances, the hardship which will constitute a defence to a claim for specific performance must have existed at the date of the contract.

[11] The basis for that passage is found in the New Zealand case which appears to be one of the earliest to discuss the impossibility defence in this country, *Nicholas v Ingram*[4] (but see *Keats v Wallis*).[5] In *Nicholas* Hutchinson J declined to hold that the defendant's indigence entitled him to invoke the defence. The Judge said: [6]

> ... The hardship that operates as a defence to such an action as this must, in general, be such as existed at the time of the contract and not such as has arisen subsequently from a change of circumstances: 31 *Halsbury's Laws of England*, 2nd ed, p 368, para 420; *Fry on Specific Performance* 6th ed, p 199, para 418. ...
>
> There are exceptional cases in which hardship subsequent to the contract has caused the Court to refuse a decree for specific performance. I was not referred to any case in which that has been done where the hardship set up was mere financial inability on the part of a purchaser to complete. The hardship that operates as a defence is "great hardship": 31 *Halsbury's Laws of England*, 2nd ed, p 369, para 419, *Fry on Specific Performance*, 6th ed, p 418, para 417. It has been referred to as "hardship amounting to injustice": *Tamplin v James* (1880) 15 ChD 215 at 221 ... In considering whether there is such hardship on the defendant, the Court must consider the hardship on the other side, too: *Tamplin v James*, *Eastes v Russ* [1914] 1 Ch 468, 480 ...; *Keats.*

[12] *Nicholas* was followed in *Baker v McLaughlin*[7] where MacArthur J summarised the authorities in the following terms:

(a) the hardship that operates as a defence must, in general, be such as existed at the time of the contract and not such as has arisen subsequently from a change of circumstances;
(b) nevertheless there are exceptional cases in which hardship subsequent to the contract has caused the Court to refuse a decree for specific performance;
(c) the hardship that operates as a defence is "great hardship", ie hardship amounting to injustice; and
(d) in considering whether there is such hardship on the defendant the Court must also consider the hardship on the plaintiff which would result if the decree for specific performance were refused.

[13] There is a distinction without a difference in Dr Spry's "sufficiently great likelihood" test and the "very substantial probability" test in *D'Arcy-Smith v Stace*[8] where other New Zealand authorities are also reviewed. But, whatever formulation is applied, it is clear law the onus of proving entitlement to the defence lies on defendants.

[14] As an aside, it is possible that an argument might be mounted that the time at which impossibility of performance should be judged is not the date of the contract but either the date on which it becomes unconditional or that on which a party fails to settle, but the authorities take a different view and, as the point was not raised by counsel, it may be noted but set aside until a case where it expressly arises.

[15] The Court accordingly turns to consider the evidence in the case, although, despite the onus, it is convenient to consider Verano's evidence before that of the defendants.

Evidence

(1) Verano

[16] Mr Flynn, Verano's property development manager, first detailed the contract into which the defendants entered making the points that the interest rate for late settlement was 16 per cent per annum and the contract specifically entitled Verano to sue the purchasers for specific performance or cancel the agreement and sue for damages (cl 12.3).

[17] He also made the point the defendants contracted to buy two lots from Verano but paid only deposits of $10,000 on each.

[18] Importantly, he emphasised that on 9 April 2010, following failure by the defendants to settle, Verano made an open offer for the defendants to settle on lot 7 using the total $20,000 deposit with Verano providing a $165,000 vendor mortgage for twelve months to fund the balance due on settlement. Interest would only run at 9 per cent per annum by contrast with the default rate under the contract. Verano would cancel the agreement on lot 4 and, provided the defendants met the obligations under the mortgage including refinancing at the end of the year, Verano would not sue them for any loss arising from cancellation of the lot 4 contract. He said in evidence at the hearing that Verano would still settle on that basis.

[19] Verano instructed a Mr Browning, an expert chartered accountant, to comment on the defendants' financial position. His evidence was hampered by omissions from the material supplied - some of which was rectified at the hearing - but he reached the view that:

> [29] ... with careful and prudent management of their financial affairs over the next twelve months [both defendants] can meet the interest payments under the Verano Properties Limited proposal submitted to them on Friday 9th April 2010. This will allow them the time to fully re-structure their affairs and dispose of assets and debt as necessary.

[20] Mr Browning elaborated on those views orally suggesting the defendants could utilise the services of a company called Tax Measurement New Zealand to defer payment of their tax or utilise current income to meet back taxes. But he acknowledged in cross-examination that the defendants' ability to meet their tax liabilities of $60,000-$70,000 each by June 2011 was subject to them selling property and entering into an arrangement with IRD.

(2) Ms de Luen

[21] Ms de Luen lives with her two children and her aged mother in a partially completed "kitset" home on the beach front at Mangawhai. The property is prone to flooding. The home is clad only in building paper. It is uninsured. Electricity comes from a builder's extension. Her family has no running hot water. Its toilet is a "Portacom".

[22] Ms de Luen is unable to find the $30,000 plus for internal fitout, insulation and other payments towards completion of the home despite being pressed for payment by the builder. Thus she finds herself in the position of working on the property to assist in its completion even though she has no building expertise. The property - apparently before some design modifications - was valued at $600,000 "as is" and $1,090,000 "as if complete" in January 2009 against the purchase price of $725,000 before she signed the Vista Verano contract. Ms de Luen's capacity to sell the property - even it is saleable - is further limited by the fact that registered proprietorship is in the name of the Blake Trust, a family trust set up by Ms de Luen and her then partner in 2001 to benefit Ms de Luen's children.

[23] Ms de Luen's financial position is further compromised in that before 2007 she bought her former partner's interest in a house at Point Chevalier Auckland which they jointly owned. She put it on the market but it took about a year to sell as it was suspected of being a "leaky home". Servicing the two mortgages was expensive and when the Point Chevalier was sold it realised only about $600,000 against a valuation of over $800,000 a year or more before.

[24] [Editorial note: para [24] omitted from this report.]

[25] She has a reasonably well settled practice in West Auckland - to which she commutes daily from Mangawhai - and also practises in Thames. The distance she travels means her fuel account is expensive and she needed to borrow $17,000 to buy a reliable car.

[26] [Editorial note: para [26] omitted from this report.]

[27] She shares chambers with Ms Jones and others. She is in arrears with her chambers expenses.

[28] She accepted that were she able to finance completion of her home and sell it at a price sufficient to meet what is owing on it and some of her accumulated debt, she may be able to benefit from the sizeable income she receives. However, at the present time she can see no means to achieve that and no ability to accept Verano's open offer.

[29] [Editorial note: para [29] omitted from this report.]

(3) Ms Jones

[30] When the defendants signed the Verano contract a family trust set up by Ms Jones in 2002 called the Fisher-Jones Trust which owned a property at 86 Barbados Drive, Albany. That was sold on 13 November 2009 and the equity of $53,845 was used to reduce the mortgage taken out to buy the property at 48 Old Mill Road, Westmere, Auckland, in February 2007. [Editorial note: further details omitted from this report.]

[31] The Old Mill Road property was "statistically worth in the early to mid $500,000s" in January 2010 but if it was sold at approximately that figure, there would be little equity after repayment of the mortgage of currently about $450,000 plus the debt to the trust of $53,845. In addition there would be commission to be paid and a penalty to the mortgagee for repaying the loan prior to due date.

[32] Ms Jones lives in rented accommodation.

[33] Ms Jones also produced an affidavit of means. [Editorial note: further details omitted from this report.]

[34] Thus she said she too was unable to accept the Verano offer and it was impossible for her to settle the defendants' Verano contract.

[35] In cross-examination, however, she accepted that were Westmere able to be sold at anything like the projected figure an equity of up to $50,000 would result of which she would be entitled to half and she is a discretionary beneficiary of the Fisher-Jones Trust which would be repaid the $53,845 owing to it.

[36] [Editorial note: para [36] omitted from this report.]

[37] She acknowledged she could increase her present annual income were she prepared to put in longer hours. If her mortgage payments on the Westmere property ceased she could meet the payments required by Verano's open offer. But she was unprepared to accept that offer given her need to refinance in a year.

Submissions

[38] It is unnecessary to detail counsels' submissions. They were brief and are incorporated elsewhere.

[39] It is, however, of some importance to note that Mr Blanchard pressed for Verano's open offer to form part of the judgment but, for pleading and other reasons, that does not appear possible.

Evaluation and conclusions

[40] The question therefore is whether either or both of the defendants have shown it is impossible and not within their power to comply with any order for specific performance. Difficulties in performance are insufficient as are financial incapacity or the fact they may now take the view they made a bad bargain. The authorities show that, other than exceptional circumstances, they must make out the impossibility/hardship defence as at 8 January 2007, the date of their contract with Verano. Exceptional circumstance arising after the date of the contract which may admit of the defence must

amount to hardship to the level of injustice, with that injustice being assessed on the basis of injustice to both parties to the bargain.

[41] Two features stand out which are common to both defendants.

[42] The first is that they entered into the contract as a speculation. They did not wish to use the two lots themselves. They did not wish to build on them. They bought, hoping and believing the land would appreciate in value, they could sell the lots after settlement at a profit and devote that profit to improving their financial circumstances - especially by paying part of their debts.

[43] It is accepted that each of the defendants is in a difficult financial position, not because they lack income, but because they have significant debt both secured and unsecured, the latter derived principally from their failure to meet their taxation obligations and their living off credit cards.

[44] But the second point to be noted is that - apart from their two payments of $10,000 at the time they signed the Verano contract - the defendants' straitened financial positions do not emanate in any way from the Verano contract. For the various reasons discussed in evidence, they have simply been living beyond their means and accumulated debt unrelated to the contract which is the subject of this litigation.

[45] Both those factors impact on whether it was impossible for the defendants on 8 January 2007 to settle the contract they were signing and whether exceptional circumstances have arisen since that date so as to make it a "'great hardship', ie hardship amounting to injustice" to all parties to order them to settle.

[46] There can be little doubt the defendants entered into a bad bargain. Even at the date of the contract, had they had a mature financial appreciation of their position, it is highly doubtful either of the defendants would or should have entered into the contract with Verano. Their asset position was not strong and, while they enjoyed a relatively substantial income, much was committed to their existing indebtedness. In those circumstances, they were unwise to contract to buy one lot, let alone two, from Verano. Even modest knowledge of the volatility of land prices coupled with the warnings of the pundits at the time as to the overheated nature of the real estate market should have led them to conclude that their belief in unending increases in land values was unsound.

[47] But, as the authorities demonstrate, that is not the test. As at 8 January 2007 the defendants, jointly and severally, were in receipt of good incomes and, had they undertaken financial rearrangements and sold assets and taken other measures, there is a high degree of probability they would have been able to meet their contractual obligations to Verano, particularly when they must have known there would be a substantial period of time before they could be called on to settle. In the event, they had 33 months in which to make the arrangements required of them to meet their contractual obligations to Verano.

[48] The only conclusion available, therefore, is that at the date they contracted to buy the two lots in Vista Verano from the plaintiff, the defendants have demonstrated no more than that they might have had difficulty in so arranging their financial affairs as to be able to settle when called upon, but, seen at that date, performance was not impossible for them.

[49] The question that then arises is whether the defendants have shown that their financial circumstances have so declined since the contract date that "great hardship" amounting to injustice would result were they now ordered to settle.

[50] In that, the Court's view is that the two defendants' positions differ.

[51] As far as Ms de Luen is concerned her financial circumstances have declined markedly since 8 January 2007. The house in which she had purchased her former partner's interest was extremely slow to sell and, when it sold, it was at a price significantly less than expected a year or more before. It may have been imprudent for her to purchase residential land as far distant from her primary source of income as it is and then to try to build on it, but it is understandable she wished to house her mother and family as well as herself, and the amount she was able to contribute to construction was significantly undermined by the reduced price she received for her house in Auckland. She and the family live in substantially substandard circumstances. They are unable to contribute much to the household's running expenses. Their situation, which will be worsened by the oncoming winter, is one which Ms de Luen is effectively powerless to improve.

[52] [Editorial note: para [52] omitted from this report.]

[53] As far as injustice to Verano is concerned, there was no suggestion it is not financially able to bear the cost of not having Ms de Luen settle with it at this stage; it may yet have a claim against her in damages. The evidence suggested the present defendants are not the only buyers in Vista Verano who are encountering difficulties in settlement - no doubt it is Verano's recognition of that position that led it to make its open offer to the defendants - but there is no suggestion the defendants' failure to settle will have a severely adverse effect for Verano at the present time.

[54] As far as the claim for specific performance against Ms de Luen is concerned, the Court therefore concludes that exceptional circumstances have arisen since the date of the contract such that it would amount to hardship and injustice to grant the plaintiff's application against her for specific performance. The plaintiff's application for such an order against Ms de Luen is accordingly dismissed.

[55] It remains to add, as far as Ms de Luen is concerned, that while Mr Browning's skilled assessment of her financial position demonstrated her possible ability to accept the Verano open offer and survive for the next twelve months, her reluctance to take on any further debt is entirely understandable, particularly when it may well do no more than postpone her severe difficulties for a year.

[56] Ms Jones' position is, however, somewhat different.

[57] [Editorial note: para [57] omitted from this report.]

[58] To expand on that, it is entirely understandable that, for the reasons she discussed in evidence, Ms Jones is extremely reluctant to sell the investment property, but she really has no choice given her other debts, her inability to fund further borrowing and her contractual obligations to Verano.

[59] In those circumstances, the only conclusion open as far as Verano's claim against Ms Jones is concerned is that she has both failed to demonstrate hardship at the date of the contract and exceptional circumstances which have arisen since that date so that it would be hardship amounting to injustice to allow Verano's claim against her.

[60] In those circumstances, the Court takes the view that Ms Jones has failed to prove her entitlement to the impossibility defence to Verano's claim for specific performance against her and the plaintiff's application is granted accordingly.

[61] Again for completeness, it must be said that Mr Browning's careful reworking of Ms Jones' financial position and his conclusions do not prevail against Ms Jones' understandable reluctance to take on further debt where it would leave her in a position where she has to refinance in twelve months time.

[62] Before concluding this part of the judgment, something needs to be said about Verano's open offer.

[63] In evidence, as has been mentioned, Mr Flynn repeated Verano's open offer and said the plaintiff was still prepared to honour it. Verano was prepared to settle with the defendants in accordance with the offer rather than the claim. Mr Browning's reworking of the defendants' financial position for the next twelve months was based on acceptance of the offer and the cross-examination of the defendants was partly directed to the advisability of their accepting it.

[64] Apart from the need to revisit the offer in twelve months' time, Verano's offer appears to have some attractive aspects for the defendants so it may be they would wish to reconsider their position in light of this judgment. However, seeing the claim was not amended and specific performance continued to be sought, not of the offer but of the 8 January 2007 contract, the Court's view is that it is not open on the state of the pleadings for it to do more than discuss the offer as it has. Put another way, the specific performance sought was of the original contract and it is therefore up to the parties, not the Court, to vary the judgment consensually if they consider that appropriate. The Court cannot give relief which was not claimed. In terms of the formal judgment, therefore, the Verano open offer is put to one side.

Result

[65] In the result the plaintiff's claim for specific performance of the contract of 8 January 2007 against both defendants is dismissed against the first defendant but granted against the second defendant.

[66] In order to give the parties an opportunity to consider their positions in light of this judgment and make arrangements for the future conduct of this claim, there will be a telephone conference between counsel and Hugh Williams J on 13 May 2010 at 9 am.

[67] As the claim will presumably continue, the Court's current view is that costs should lie where they fall, but questions of costs can be discussed at the conference.

[68] There is probably no more basis in principle to suppress details of barristers' finances than those of any other defendant, but, on the other hand, there does not currently seem to be any reason why the defendants' personal details should be in the public domain. There will therefore be an order suppressing from publication other than to the parties and legal publications, of the details of the defendants' financial position appearing in [24], [26], [29], [30], [33], [36], [52] and [57] of this judgment. That order will be reviewed on 13 May 2010.

A. The plaintiff's claim against both defendants for specific performance of their contract of 8 January 2007 is dismissed against the first defendant but granted against the second defendant.
B. The future conduct of the proceeding and costs is to be discussed as set out in [65] and [66] of the judgment.
C. There will be an order suppressing - other than to the parties and legal publications - any details of the defendants' financial positions appearing in [24], [26], [29], [30], [33], [36], [52] and [57] hereof. That order will be reviewed on 13 May 2010.

FOOTNOTES

1 Burrows Finn and Todd *Law of Contract in New Zealand* (3rd ed, 2007) at [2.1.2].

2 Spry *The Principles of Equitable Remedies* (8th ed, 2010) at 127-129.

3 *Snell's Equity* (31st ed, 2005) at 374; [15]-[41].

4 *Nicholas v Ingram* [1958] NZLR 972 (SC) at 973.

5 *Keats v Wallis* [1953] NZLR 563 (SC).

6 *Nicholas v Ingram* at 973-974.

7 *Baker v McLaughlin* [1967] NZLR 405 (SC) at 414.

8 *D'Arcy-Smith v Stace* (2003) 4 NZ ConvC 193,771, (2003) 10 TCLR 788 (HC) at [26].

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