Hickman v Turn and Wave Ltd

Supreme Court of New Zealand SC46/2011; [2012] NZSC 72
7, 8, 9 November 2011; 9 August 2012
Elias CJ, Tipping, McGrath, William Young and Anderson JJ

Contract – Illegal contract – Doctrine of tainting – Knowledge – Constructive knowledge – Observation. – Illegal Contracts Act 1970.

Practice and procedure – Appeals – New issue raised at late stage – Whether caused prejudice to any party – Nature of prejudice.

Securities – Securities Act 1978 – Meanings of "security", "debt security", "consideration", "issuer", "otherwise owing", "subscribe" and "equity security" – Whether transactions "in respect of estate or interest in land" – Whether security could have more than one issuer – Whether issuer, offeror and alloter had to be same party – Whether knowledge to be attributed to party – Securities Act 1978, ss 5, 33, 37 and 37AL.

Three development companies set out to raise money for a number of buildings. As a condition of bank loans they had to pre-sell a number of apartments. They engaged a group of companies known as Blue Chip to do so. Blue Chip sold apartments off the plans to investors through arrangements which involved entry into a sale and purchase agreement (SPA) with the developers as well as Blue Chip's financial products. There were three different financial products which varied in their details: the joint venture agreement (JVA); the premium income product (PIP); and the put and call agreement (PAC). These sales generated underwriting fees for Blue Chip as well as giving it the substantial part of any capital gains derived from the intended further sale of the apartments. The investors received fees, which under the JVA and PIP were functionally similar to interest and in the case of the PAC product involved a sharing of Blue Chip's underwriting fee. The intention was that second purchasers would be found for the apartments but if this did not occur, the investors were committed to purchase of the apartments. The schemes all depended for their success, from the point of view of the investors, on continued increases in property prices and on Blue Chip honouring its commitments. In the event, property prices fell and Blue Chip became insolvent. The investors claimed that the JVA, PIP and PAC products amounted to "securities" under the Securities Act 1978. It was common ground that, if that were the case, the products had been offered without a prospectus and without a trustee, in which case they had been offered in breach of the Act and were potentially void. The investors sought to impeach the closely associated agreements for sale and purchase they had entered into with the developers on the basis that the improper marketing by Blue Chip rendered unenforceable the allotment of the securities and the associated subscription for such securities. A "debt security" was defined under s 2 as "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". An "issuer" was defined as "the person on whose behalf any money paid in consideration of the allotment of the security is received". "Money" was defined as including "money's worth" and "subscribe" was defined as "purchase and contribute to, whether by way of cash or otherwise". In the High Court, the developers successfully argued that Blue Chip was not an "issuer" because the deposits had gone to the developers and not to Blue Chip and had not been received on behalf of Blue Chip. On appeal, the Court of Appeal held that the words "otherwise owing" were to be construed ejusdem generis with "deposited with" and "lent to" and that money "otherwise owing" was confined to obligations to repay to a subscriber money previously paid by the subscriber to the issuer. The investors appealed to the Supreme Court and the Court called for argument as to whether the developers were issuers by virtue of receiving via Blue Chip the consideration for the allotments in the form of the deposits and the entry into obligations under the sale and purchase agreements.

Held: (unanimously) 1 Sections 33 and 37 of the Securities Act 1978 and the associated definitions of "security" and "debt security" were, despite their breadth, to be read in a way which accorded with the ordinary meaning of the words used and not read down. The words "or otherwise owing" were of the widest ambit but were qualified by the provisions of s 5 (see [37], [45], [46], [49], [53], [124]).

2 The Blue Chip products came within the definition of "debt security" because they conferred on the investors the right to be paid money that had been paid to them by Blue Chip. Although that money had not been deposited with, or lent to, anyone it was "otherwise owing" (see [37], [45], [46], [49], [53], [124]).

Culverdon Retirement Village v Registrar of Companies (1996) 1 BCSLR 162 (CA) approved.

Australian Softwood Forests Pty Ltd v Attorney-General of NSW (1981) 148 CLR 121, (1981) 36 ALR 257 referred to.

3 The transactions entered into between the investors and Blue Chip in relation to the apartments were not ordinary purchases of land and Blue Chip's obligations to the investors in relation to the apartments were not unexceptional terms ancillary to the purchase of an interest in land. From the investor's point of view, the apartments were of only peripheral significance. Such profits as the investors could expect to derive depended on Blue Chip honouring its promises. The exemption in s 5(1)(b) of the Securities Act did not apply (see [61], [81], [83], [124]).

4 A non-technical approach was justified in identifying whether a party was an issuer under the Securities Act. Under the PIP and PAC agreements, Blue Chip would be credited, in relation to the developer, with any money paid by the investor. Blue Chip also received benefits otherwise than in cash, or as money's worth. Entry into the sale and purchase agreements conferred benefits on Blue Chip such as control of the apartments and facilitating the payment of underwriting fees. Entry into the SPAs therefore constituted subscription and Blue Chip was an issuer (see [65], [66], [67], [106], [124]).

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

5 The developers were issuers because 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. The developers thus received money (being deposits) and money's worth (in the form of the obligations under the agreements). The SPAs were therefore subscriptions within the s 2 definition. The developers were to repay any money received and cancel the SPAs under s 37(5) (see [112], [116], [119], [125], [126], [127]).

6 Whether knowledge and actions of one party were to be attributed to another was controlled by the policy of the legislation rather than by the details of the formal documents between the parties. Blue Chip had been the agent of the developers in the sense that it had acted on the developers' behalf in marketing the apartments and the developers had known of either the detail or the substance of the investment products which were being marketed (see [98], [99], [100], [124]).

Meridian Global Funds Management Asia Ltd v Securities Commission [1995] 3 NZLR 7 (PC) applied.

Nathan v Dollars & Sense Ltd [2008] NZSC 20, [2008] 2 NZLR 557 applied.

Scott v Davis [2000] HCA 52, (2000) 204 CLR 333 referred to.

Colonial Mutual Life Assurance Society Ltd v Producers and Citizens Co-operative Assurance Co of Australia Ltd (1931) 46 CLR 41, [1932] ALR 73 referred to.

Morgans v Launchbury [1973] AC 127, [1972] 2 All ER 606 (HL) referred to.

7 From the point of view of the investors, the Blue Chip products and the sale and purchase agreements were an integrated package in the cases where the SPAs had been executed at the same time as or after the corresponding Blue Chip agreement had been entered into. The promises and payments made by the investors had been pursuant to and in that sense part of the consideration for the promises made by Blue Chip. The subscriptions in this case encompassed the actions of the investors in entering into the SPAs. The SPAs and the payments made under them were therefore allotments of a security made without a registered prospectus and were invalidated by s 37(4) of the Securities Act. The exemption under s 5(1)(b) did not apply (see [104], [105], [124]).

Hurst v Vestcorp Ltd (1988) 12 NSWLR 394 (CA) referred to.

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

Result: Appeal allowed.

Observations: (i) (per totam curiam) The marketing of real property may result in a money liability by the vendor to the purchaser if the property is misrepresented. The potential for such liability is so much an ordinary incident of transactions involving the sale of real property as to be naturally within s 5(1)(b). Straightforward consumer transactions are not caught by the

Securities Act concept of what is involved in offering debt securities to the public (see [58]).

(ii) (per totam curiam) The issuer and offeror of securities are not necessarily the same person. The Act provides separately for "issuers", "offerors" and "allotters". A strictly contractual approach to consideration is not therefore required (see [116]).

(iii) (per Elias CJ, McGrath, William Young and Anderson JJ) When considering whether late consideration of an issue which has not been advanced earlier may cause prejudice, the court is concerned with prejudice resulting from the possibility that a party might have led different evidence or otherwise conducted its case differently, and not with issues of litigation strategy, for example that a party might have settled earlier if the point had been taken earlier (see [113]).

(iv) (per Tipping J) The common law doctrine of tainting is not affected by or amenable to relief under the Illegal Contracts Act 1970 but, in the present circumstances, it is amenable to relief under the Securities Act. The collateral contract and the primary contract in this case were interdependent. The primary contract was the means of financing the collateral sale and purchase contract. Where a third party stands to benefit from the contravening transaction, that party should suffer the same consequences as the party who benefits from the primary contract. It serves the policy of the Securities Act if a party to a tainted contract cannot avoid the consequences by demonstrating ignorance of a relevant matter of fact or law. If knowledge is required, it is sufficient that the party knows, or ought to know of the facts which give rise to the illegality; it is not required that the party knows that the facts constitute unlawful conduct (see [134], [135], [136], [145], [148], [149], [152], [156], [160]).

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

In re Trepca Mines Ltd (No 2) [1963] Ch 199, [1962] 3 All ER 351 (CA) discussed.

Other cases mentioned in judgment

Abbott v UDC Finance Ltd [1992] 1 NZLR 405 (CA).

AIC Merchant Finances Ltd, Re [1990] 2 NZLR 385 (CA).

Archbolds (Freightage) Ltd v S Spanglett Ltd [1961] 1 QB 374, [1961] 1 All ER 417 (CA).

Culverden Retirement Village Ltd v Registrar of Companies [1997] 1 NZLR 257 (PC).

DFC Financial Services Ltd v Abel [1991] 2 NZLR 619 (HC).

Fisher v Bridges (1854) 3 E & B 642, [1854] 118 ER 1283.

GE Custodians v Bartle [2010] NZSC 146, [2011] 2 NZLR 31.

Heald v O'Connor [1971] 1 WLR 497, [1971] 2 All ER 1105.

Icon Central Ltd v Collingwood HC Auckland CIV-2008-404-7424, 25 November 2009.

Lester v Greenstone Barclay Trustees Ltd [2010] 3 NZLR 67 (HC).

Scott v Brown, Doering, McNab & Co [1892] 2 QB 724 (CA).

Securities and Exchange Commission v Bailey 41 F Supp 647 (SD FLA 1941).

Securities and Exchange Commission v Howey Co 328 US 293 (1946).

Spector v Ageda [1973] Ch 30 (Ch).

United Housing Foundation Inc v Forman 421 US 837 (1975).

Appeal

This was an appeal by Neil Tony Hickman and others, first appellants, David John Lester and others, second appellants, Anthony Collingwood and others, third appellants and Norman and Marie Herrick, fourth appellants from the judgment of the Court of Appeal [2011] NZCA 100, [2011] 3 NZLR 318, dismissing or adjourning their appeals from three judgments of Venning J: *Lester v Greenstone Barclay Trustees Ltd* [2010] 3 NZLR 67 (HC); *Hickman v Turn and Wave Ltd* HC Auckland CIV-2008-404-5871, 25 November 2009; and *Icon Central Ltd v Collingwood* HC Auckland CIV-2008-404-7424, 25 November 2009, dismissing their applications for declarations as to the validity of their cancellation of individual sale and purchase agreements, leave to appeal having been granted by the Supreme Court [2011] NZSC 102, on the questions: (1) Did the marketing by Blue Chip companies and sales agents of the Blue Chip investment products amount to offers to the public of equity and/or debt securities for the purposes of s 37 of the Securities Act 1978? (2) If so, is the exemption in s 5(1)(b) applicable? (3) If the answers to questions (1) and (2) are favourable to the investors, does this impeach the ability of the developers to enforce the agreements for sale and purchase on the basis that they: (a) constituted part of the relevant allotments and were thus void and of no effect under s 37(4); or (b) were tainted by their association with those allotments and thus illegal?

PJ Dale, *NR Campbell* and *DW Grove* for the first to third appellants.
SH Barter for the Herricks.
DJ Chisholm and *GP Blanchard* for Turner and Waverley Ltd (formerly Turn and Wave Ltd).
DJ Neutze for Greenstone Barclay Trustees Ltd.
B O'Callahan for Grafton Projects Ltd (formerly Icon Central Ltd).

Campbell for the appellants: The investment products were securities. Blue Chip cannot claim the benefit of the agents' work while disclaiming responsibility for what they said. We rely on the definition of "debt security". Blue Chip marketed the apartments as a financial package. There were three types: a joint venture in which Blue Chip undertook to make payments to the investors as a return on investment; the PIP agreements; and the PAC agreements. The Court of Appeal shows at [28] how Blue Chip marketed its own services as "more akin to a financial product than a standard property investment". This was accurate and brought them under the Securities Act 1978. The arrangements contemplated that licensed real estate agents would be used, but they were not and the High Court held that the developers knew that and impliedly authorised it. The letter of authority from some investors to Blue Chip authorised Blue Chip to apply for finance, find property, place deposits and draft agreements for execution by investors, including the "call" agreement; that is, the PIP agreement. Blue Chip found the properties, and a sales person drew up the analysis setting out the expected return. It has never been argued that Blue Chip on behalf of the investors performed any act actionable by the developers. Blue Chip sent investors documents setting out the transaction "designed to provide a secure passive income stream". The investors were entitled to interest on the capital provided by the investor and for which the investor raised finance. This eliminated the cost to the investor of financing simply an indemnity and was effectively an indemnity against that cost. The procurement fees then became the real return along with the portion of capital gain to which the investor was entitled and the "initial contribution". There was thus a promise of repayment of the initial contribution. The fees and added costs could only be recovered if property prices continued to rise at the rate they were doing in the early 2000s. The transaction therefore related to real property but the transaction between Blue Chip and the investor was a purely financial one. The return from capital gain was a small proportion of the total return, the real return was the from the procurement fee. Venning J in *Icon Central Ltd v Collingwood* HC Auckland CIV-2008-404-7424, 25 November 2009 at [111]–[118] is not quite correct. The sale and purchase was signed first and the joint venture agreement later, so an investor who refused to sign the JV agreement became solely responsible for the purchase. The tables set out the payments investors would receive from Blue Chip, the indemnity for interest and the procurement fee, until the property was sold whereupon the initial contribution would be returned plus a small portion of the capital gain. Turn and Wave Ltd (TWL) says that it was not aware that Blue Chip sales agents were doing the marketing but this is contrary to the findings in the Courts below, see Venning J at [94], [105] and [106] where it was found that TWL knew the apartments were to be sold by Blue Chip sales agents. Despite these findings of fact, Venning J held that TWL did not have actual knowledge of the details but did know that the apartments were to be marketed in conjunction with a financial package. In relation to Icon, it was also found that it knew of the details. If knowledge cannot be imputed to Greenstone and TWL, they still knew enough to know that this was a financial product, not simply the joint purchase of a property (CA at [144]). TWL relies on Venning J at [124] but all that passage does is record the evidence of one witness. Icon knew of the procurement fee and interest indemnity but the findings were that Greenstone and TWL did not. The reference to a 16 per cent return refers to the return on the deposit only, assuming that Blue Chip would exercise its options or that the investors would never have to settle. They certainly knew that this was not a mere sale of property. In relation to allotment, the argument is that the sale and purchase agreement was necessary to create the securities. The question was whether they could nonetheless be severed. Participation in allotment comes from knowledge about marketing in conjunction with the financial product. The apartments were fungible to some extent. The joint venture product included a sale and purchase agreement and noted that the apartment was sold subject to lease. The agreement provided that a company was to be formed to be trustee for the joint venture of which the investor would be the sole shareholder and director. By a deed of nomination the investor nominated the company to take title to the property. If the property was sold, cl 12.2 provided that the joint venturers would resolve to sell the property and on sale would receive distribution of their respective interests. "Interest" was defined to mean shares as tenants in common recognising the initial contribution. Clause 6.10.4 provided for the net proceeds of sale, "net proceeds" meaning the proceeds less all costs attributable to the property. The investor received 5 per cent and the Blue Chip company 95 per cent. Clause 12.2 was not a promise by Blue Chip to pay the investor anything, it was a simple distribution of sale proceeds, so was not itself a debt security but in parallel Blue Chip was making separate promises as to the return on investment. We submit that there does not have to be a repayment for the arrangement to qualify as a debt security but if it is necessary, there was a repayment.

The PIP was an income only product. The PIP agreement was conditional on an investor executing a sale and purchase agreement; the investor had to pay the deposit to the vendor. The investor granted Blue Chip an option and Blue Chip paid the option fee until it exercised the option. The fee was calculated as a return on the deposit. The deed of nomination provided that if Blue Chip exercised the option, its nominee reimbursed the investor all money paid by the investor to the vendor. If Blue Chip did not exercise the option the investor had to settle and Blue Chip would reimburse the investor all costs including interest on borrowing. The investor could not sell the property and had no entitlement to a share in any capital gain. The PAC product involved Icon only, under this agreement the investor granted Amelia an option to purchase for a fee and also had the option to require Amelia to purchase the property. In either case, Amelia would pay the investor the cash deposit paid by the investor under the sale and purchase agreement. As to Greenstone, Mr Abel-Pattinson was aware in general terms of the existence of the joint venture product. As to TWL's knowledge, see the meeting minutes at [148] of the Court of Appeal judgment, especially the note that although PIP purchasers sign a PIP sales pack, the Turn and Wave sale and purchase agreement is to be signed at the same time, along with the addendum and lease. The knowledge that the transaction was not a normal sale of property assists the investors on the agency issue. The sale and purchase agreements were not conditional on or tied to the investment products (CA at [256] and [260]). This meant that if there were any defects in the investment product, it did not affect the validity of the sale and purchase agreement. Investors knew that they might be required to settle (CA at [223] and [237]). This is not relevant to whether there has been a breach of the Securities Act which is intended to ensure that investors are properly informed of the risks through a prospectus. The Act provides for the consequences of there being no prospectus. These transactions were marketed as investments and the purchasers were investors. The definition of "security" is wide (*City Realties Ltd v Securities Commission* [1982] 1 NZLR 74 (CA) per Cooke J) especially when s 2 defines "money" as including "money's worth". The words "otherwise owing" make clear that the right to be paid does not have to arise from the investor depositing money with or lending money to the person who is to pay the money. "Money's worth" means something treated by the parties as equivalent to money, it does not mean any chattels capable of exchange. This was deliberate, in order to avoid schemes being designed to circumvent the previous narrow definitions. The wide definition is then pared back by the exceptions in s 5, and by those created by regulation or granted by the Financial Markets Authority. The definition in s 2D(1) consists of an initial definition which is then extended to "include" an equity security and a debt security. Hence if the transaction falls within the definition of an equity security or a debt security, there is no need to show that it falls within the opening part of the definition and that there was participation in the security. The classic debt security is a bank account which would not fall within the initial definition of "security".

Sole owners or members of a group of five owners are not covered as they are sufficiently protected by control and ownership. The mere fact of ownership does not prevent transactions from being within the Act. There was an equity security arising from the right to hold shares in the joint venture company. Before the shares were issued, there was an issue of the right to hold all the shares. An equity security is defined in s 2 as an "interest in or right to a share in a company". The Court of Appeal held that the shares were the equity securities (at [304]) but they were not offered to the public. If the Court of Appeal is correct, the Securities Act would not apply to options over shares, warrants and so on. The Court of Appeal rejected Venning J's opinion that the fact that the company was only to hold real property took it outside the Act. The debt security arose from the rights to interest payments and procurement fees, provided that the investor paid money or money's worth in consideration for that right. The investors here were investing money in return for an income stream, this is not the case with concert or airline tickets with a right to a refund. The Court of Appeal's holding at [312]–[316] that a repayment obligation is required for a debt security is contrary to the Court of Appeal decision and Privy Council dictum in *Culverden Retirement Village Ltd v Registrar of Companies* (1996) 1 BCSLR 162 (CA); [1997] AC 303, [1997] 1 NZLR 257 (PC). The Court of Appeal read into the Act a limitation not expressed in the detailed hierarchy of exceptions under the Act. Nor does the requirement fit in with the definitions of money as including "money's worth" or of an issuer, how can an issuer repay money's worth? An annuity is not repayment of the capital invested. The fallback position is that under the joint venture that is what occurred anyway, an income investment followed by repayment of principal. The PIP agreement focuses on the return on the deposit plus the right to return of the deposit if the option is exercised or of the costs of settling if the option is not exercised. The Court of Appeal says at [325] that it was not a debt security as there was no obligation to repay money contributed by investors. The PAC agreement gave the investor reimbursement as under the PIP agreement and PAC fees for the right granted to Amelia and the right to receive interest. Section 5(1)(b) does not apply as the transaction is not "in respect of" an estate of interest in land. An ordinary purchaser of land is sufficiently protected by the ordinary law, there is no need for the disclosure regime under the Securities Act. "In respect of" is wider than "to" and applies to rights commonly arising under a sale and purchase agreement, but does not include a financing transaction which involves a sale and purchase agreement, see the Privy Council in *Culverden*, at 305 of the AC report. It is clear from counsel's argument that the phrase "in respect of" may have a wide meaning in other statutes but not in this. The Privy Council was correct not to apply it to an ordinary purchase of land. If "in respect of" were to have a wide meaning, *Culverden* would have been differently decided and any loan for the purpose of purchasing land would be outside the Act. The rights under the joint venture agreements were not merely ancillary to the sale of land.

Were the SPAs part of the relevant allotments and thus void under s 37(4)? The allotment was the entry into the agreements that gave rise to the securities: *Re AIC Merchant Finances Ltd* [1990] 2 NZLR 385 (CA); *DFC Financial Services Ltd v Abel* [1991] 2 NZLR 619 (HC) at 626; *Braemar Lodge 2004 Ltd v Owers* [2010] NZCA 300, (2010) 10 NZCLC 264,703. Section 37(4) means that those agreements are invalid and of no effect. The agreement invalidated by s 37(4) consists of both the Blue Chip agreement and the sale and purchase agreement. The rights that constituted securities could not arise without the sale and purchase agreements. The PIP agreement was conditional on entry into the sale and purchase agreement but not vice versa. The Illegal Contracts Act 1970 does not apply (s 4(5)) and nor does the special regime under the Securities Act. The Act makes the transaction void and so it is hard to see how the courts can sever the sale and purchase agreement to save it. The appellants are not claiming damages for breaches of the Act but simply to be returned to the position the position they were in beforehand, relying on *Hurst v Vestcorp Ltd* (1988) 12 NSWLR 394 (CA). *DFC v Abel* and *Abbott v UDC Finance Ltd* [1992] 1 NZLR 405 (CA) can be distinguished. In those cases, the investor appointed agents to find horses, the reverse of the present facts. In those cases, the question was whether the illegality of the partnership arrangement affected the related loan transaction. In *Hurst v Vestcorp* and the present case, the question is whether a composite transaction that it is illegal should be severed into legal and illegal parts.

Even if the sale and purchase agreements are not part of the allotment, they are subject to the common law of tainting. For that it is not necessary that the defendant parties knew that the Act was being breached, merely that they knew of the facts which constituted the breach (*J M Allan (Merchandising) Ltd v Cloke* [1963] 2 QB 340 (CA)). If the sale and purchase agreements were entered into for the purpose of assisting the promotion of illegal investment products, then the parties are participants in illegal acts. Ignorance of the law is no excuse. Greenstone and TWL had no actual knowledge, but knowledge can be imputed. The Court of Appeal held that the knowledge had been acquired outside the mandate. The question is what was the agents' mandate? Greenstone and TWL knew that this was the sale of an investment not just of land. In that case, the agents' actions were within the scope of what they were engaged to do, to obtain purchasers for an investment product. The fallback position is that although the agents were just canvassing agents, they were the only people undertaking this task, they were in the shoes of the principal for the purpose of offering securities. The argument in *Nathan v Dollars & Sense Ltd* [2008] NZSC 20, [2008] 2 NZLR 557 applies here also as well as to severability. The question is whether the risk which eventuated was sufficiently close to the agents' task to be a risk the principal should bear. [Reference also made in printed case to: *Agnew v Pardington* [2006] 2 NZLR 520 (CA); *Carney v Herbert* [1985] AC 301 (PC); *Equiticorp Industries Group Ltd v The Crown (No 47)* [1998] 2 NZLR 481 (HC); *Governments Stock Securities Investment Co Ltd v Christopher* [1956] 1 All ER 490; *Jessett Properties Ltd v UDC Finance Ltd* [1992] 1 NZLR 138 (CA); *Lloyd v Grace, Smith and Co* [1912] AC 716 (HL); *Permanent Trustee Australia Co Ltd v FAI General Insurance Co Ltd* [2001] NSWCA 20, (2001) 50 NSWLR 679; *Portland Holdings Ltd v Cameo Motors Ltd* [1966] NZLR 571 (CA); *Priddle v Accident Compensation Corporation* (2007) 8 NZELC 98,558 (CA); *Trustees of KD Swan Family Trust v Universal College of Learning* CA255/02, 23 September 2003; *Tinsley v Milligan* [1994] 1 AC 340 (HL).]

Barter for the Herricks in the *Icon* appeal: because of the put and call, the Herricks were in a position where they could always demand repayment. The deposit was clearly paid on behalf of the Blue Chip entity (see Venning J at [239]). It sits with the stakeholder and was an advance on the price. If the Blue Chip company takes over under the deed it benefits from the deposit. This makes the PAC transaction different from the PIP and there is a direct obligation on the Blue Chip entity to repay the deposit at the demand of the Herricks. The Courts below said that it was not a debt security as the deposit was not paid to the issuer but the issuer had the benefit of the deposit and therefore it was the party on behalf of whom the money was received. As to the doctrine of tainting, the Court of Appeal dealt with this by adapting *Portland Holdings v Cameo Motors*. Both parties have relied on what they argue is the ratio of *Portland*. Is it necessary for one contract to lead to the other? There are references in *Portland* to mere "association" of contracts. [Reference also made in printed case to: *Culverden Retirement Village* (PC).]

Neutze for Greenstone Barclay: Greenstone was incorporated for the sole purpose of the Barclay development and it had knowledge of the transactions at a general level only (see Venning J at [132] and following). The agency was limited to introducing purchasers so misdescriptions of property would bite, but not misdescriptions of the financing. The appellants do not challenge the factual findings, but say that the respondents knew that Blue Chip sales agents would be marketing properties in conjunction with Blue Chip financial products. That goes beyond the findings in the lower Courts. The Judge found that the directors were not aware of the details of the Blue Chip joint venture agreements and their significance did not register. The Court of Appeal found that there was no reason to find that Greenstone had actual or imputed knowledge of the details of the joint venture agreements (at [209]). General knowledge that there were transactions falls short of what is required for tainting. Under the joint venture agreements, the joint venture company, not the issuer, Blue Chip, was required to make the payments. Severability of provisions which are invalid or unenforceable is provided for in the agreement, which means that any transactions found to be debt securities can be severed. It was an obligation, not a right, for the investor to hold all the shares in the company and hence there was no equity security (see CA at [305]). The right to hold the shares and appoint directors was not a right offered to the public, it could only be exercised by the investor. The shares were allotted by the company, the investor signed an incorporation document. In substance, the investor got an interest in the joint venture company. As to the PIP agreements, the option fee was paid in consideration for the grant of the option. In *Culverden*, the transaction was in substance a licence to occupy because of the inevitability of the buy-back provision. It was also a contributory scheme so it did not come within s 5(1)(b). The use of "otherwise owing" in the definition reinforces the use of ejusdem generis. There are conflicting authorities but in this case if it is just an obligation to pay money and not payment to the issuer with a repayment obligation, this goes well beyond what was intended to be a debt security. It is what the documents say that determines whether something is a security. The Court should not look at extraneous material (*Society of Lloyd's v Hyslop* [1993] 3 NZLR 135 (CA) at 141; *Culverden*). Certainty is important and the consequences of a breach of the Securities Act are potentially severe, including for people who are not before the Court (CA at [273]). In *Culverden*, the Privy Council did not consider "in respect of" and inserted the words "ordinary" and "unexceptional" which are not there. In *Culverden* there was a payback. Venning J said that if a contract was ancillary to a sale and purchase agreement, then it was in respect of the agreement. The discussion of the contributory scheme in *Culverden* was obiter but the Privy Council did consider it. A contributory scheme implies a level of control; if there are multiple parties then any one has less control. In the present case, the investor has control of the company so s 5(1)(b) should apply. The investor also got the right to tangible property and it was likely that solicitors would be involved in the land transactions and so should be able to advise on the prospectus (see Venning J at [429]). There are plenty of authorities on the meaning of "in respect of". It is the widest of phrases (see, for example, *Trustees, Executors and Agency Co Ltd v Reilly* [1941] VLR 110 at [2.27]). [**MCGRATH J** referred to *Phonographic Performances (NZ) Ltd v Lion Breweries Ltd* [1979] 2 NZLR 252 (CA).] It has been argued that the ejusdem generis rule should have been applied in *Culverden* (see Watts [1996] NZ L Rev 275; [1997] NZ L Rev 319) and that *Culverden* has been seen as a case that might have turned on its special facts (Dawson [2002] NZ L Rev 279). As to the joint venture agreement: the documents must be examined to see whether a security has been issued; there was on the documents an offer of a joint venture interest to acquire a residential apartment on the terms and conditions of the joint venture agreement; the interest payments and procurement fee are not debt securities and *Culverden* is distinguishable; the interest payment and procurement fee were offered in respect of a sale of an interest in land within s 5(1)(b). The Securities Act was not intended to apply to a real property investment. The argument that it was a debt security depends on singling out two terms from the detailed provisions of the joint venture agreement (see Venning J at [256]). Further, neither of these terms meets the usual characteristics of a debt security. The investor is not a subscriber as it does not pay money to the joint venture company for the debt security. The joint venture company is not an issuer because it does not receive any moneys for the debt security. There is no right of participation, which is required as the specific definition of debt security is coloured by the introductory part of the definition. The idea of a debt security includes the idea of participation not just owing money. As to the PIP agreements, offer of an option is not the offering of a security; it cannot be paid back. Blue Chip obtained an interest in land. An option to sell an estate or interest in land is in respect of that estate or interest. The perpetual bond is a participatory security and not debt security, as there is no right to repayment. A time share might well be a contributory scheme and can be structured so that it is a mere licence to occupy. An annuity is a participatory security but not a debt security. Venning J records at [225] the concession in the High Court by the appellants that sale and purchase agreements are exempted from the Securities Act but argued that they are tainted by the alleged illegality of the Blue Chip investment products. This concession was properly made.

It is the allotment of the security that is avoided in a case of breach of s 37(1), so it is essential to identify the allotment of the security. It will usually be the contract formed by the issuers' acceptance of the subscriber's offer for a security (*DFC v Abel*). In this case, it is the entry into the joint venture agreement. In respect of the PIPs, it will be the entry into the PIP agreement and deed of nomination. It is therefore those agreements that are invalidated by s 37(1) and (4) (see discussion of *Hurst* in *DFC v Abel*; *Abbott v UDC Finance Ltd*). The courts will not cast the net of invalidity too wide to avoid injustice to innocent third parties (*Abbott v UDC* at 413). Greenstone, its directors and its bankers are innocent third parties in the *Abbott* sense. The appellants rely on *Hurst v Vestcorp* but in that case the loan agreement and the investment contract were one transaction (see *DFC v Abel* at 631). In this case, there are independent contracts involving independent parties. One cannot imply a term that the sale agreements are dependent upon the validity of the investment agreement (compare *DFC v Abel* at 630). There is no authority for the proposition that there is a principle of non-severability outside a contractual analysis of express and implied terms. The Court of Appeal held that the sale and purchase agreements were independent of the Blue Chip agreements and no question of severability arose (at [358]). This is not challenged by the appellants. The Illegal Contracts Act does not apply but there is the special regime in the Securities Act for granting relief when securities were allotted in breach of s 37. The scheme makes the issuer and its directors liable to repay the investors and allows for relief orders so that the allotment is treated as validly made. Section 37AL confines orders the court may make, especially s 37AL(2), which provides an exclusive set of remedies. So, if the appellants are allowed to resile from the concession that there was no allotment of a security in respect of the sale and purchase agreements, they are caught by s 37AL(2). [Reference made in printed case to: *Agnew v Pardington*; *Vasan v Medical Council of New Zealand* [1992] 1 NZLR 310 (CA); *Shell New Zealand Ltd v Commissioner of Inland Revenue* (1994) 16 NZTC 11-303 (CA); *Nowegijick v R* [1983] 1 SCR 29; *Trustees Executors and Agency Co Ltd v Reilly* [1941] VLR 110; *Asher v Seaford Estates Ltd* [1950] AC 508, [1950] 1 All ER 1018; *Paterson v Chadwick* [1974] 1 WLR 890; *Tatam v Reeve* [1893] 1 QB 44; *Nicholl v Ipsen* 204 NE (2d) 807 (1955); *Polikoff v Levy* 204 NE (2d) 807 (1965); *Brothers v McMahon* 115 NE (2) 115 (1953); *State of Ohio v Silberberg* 139 NE (2d) 342 (1956); *Laybutt v Amoco Australia Pty Ltd* (1974) 132 CLR 57; *Murray v Scott* [1976] 1 NZLR 643 (SC); *Re AIC*; *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410, (1978) 21 ALR 585.]

Chisholm for Turn and Wave Ltd: I wish to make submissions on tainting and agency. The plaintiff seeks a declaration the security is unenforceable under s 37AL. It is not disputed that TWL knew that Blue Chip marketed an investment product (see Venning J at [106]), but it did not know that the associated contracts were anything other than an ordinary property investment. The meeting minutes (see CA at [148]) did not bring the transaction under the Securities Act, in fact were not even enough to put TWL on inquiry. Habitual investors are not caught under the Act and that may be what "professional investors" means. TWL expected estate agents to be involved but that is not relevant to defining the scope of the agency. The question is whether knowing that there was an investment product which appeared to be a standard transaction fixes TWL with knowledge that it was an unusual transaction or whether it was put on inquiry. The underwriting agreement goes no further than selling the property and the authority was only to introduce, not to agree to terms on behalf of the principal. A real estate agent has ostensible authority to make statements describing the property but not to arrange finance. The Blue Chip agents were acting on behalf of Blue Chip, on behalf of the investors in finding property and for the developers. The Court of Appeal refers at [305] to the investors incorporating companies. The investors were fully informed as to the nature of the product and were advised to look at the performance of the developer and of Blue Chip and at the value of the underlying asset. Each PIP investor received a product description which referred to the risks, including that the property market might fall and which explained that the risk and return were greater than for a deposit account. Venning J at [425] summarises the evidence of what Mr Hutchinson knew. Mr Hutchinson had advice, was a real estate agent and took plenty of time. It would have been possible for him to sign the sale and purchase agreement but not the joint venture agreement. The documents make clear that they are separate transactions with separate risks. Any option to buy has to have an underlying sale and purchase agreement. The substitution clause was to enable TWL to substitute an apartment of equal value in case the agents sold the same apartment twice.

As to agency and vicarious liability, the agents acted outside the scope of the task that the underwriter had been appointed for: see Venning J at [143] and [153]. The appellants acknowledge that the Blue Chip agents acted on behalf of Blue Chip. Nonetheless, the appellants argue vicarious liability on the part of TWL. In *Dollars & Sense*, what Rodney Nathan did was within the scope of the authority. If the agent has a separate business offering advances, that does not bring it within the scope of the task. The scope of agency for vicarious liability and for representations must be the same. As to imputed knowledge, scope of authority is not the defining issue but is a starting point. The principal is only imputed with knowledge the agent gained within scope. Knowledge gained when acting on behalf of Blue Chip or of investors cannot be imputed to TWL: see *Jessett Properties Ltd v UDC Finance Ltd* [1992] 1 NZLR 138 (CA); *El Ajou v Dollar Land Holdings plc* [1994] 2 All ER 685 (CA). Solicitors do not usually sign or bind unlike directors as agents of a company. The question is to what extent the agent stands in the shoes of the principal but there may be special duties to communicate, for example, a solicitor has a greater duty to communicate than other agents. Some agents have authority to commit the principal; for example, insurance agents who can negotiate and bind. In these cases, there is no need to impute knowledge as the agent is binding the principal (see *Permanent Trustee Australia Co Ltd v FAI General Insurance Co Ltd* [2001] NSWCA 20, (2001) 50 NSWLR 679 at [89]). Watts in "Imputed knowledge in agency law" [2005] NZ L Rev 307 refers under the heading "Delegation of task" to Handley J's statement which applies when the agent has power to commit. Handley J distinguished between mere notice cases and duty to disclose cases. Where the agent can bind an insurer it has a duty to disclose to the insurer. *Bowstead and Reynolds on Agency* (19th ed) at 1.004 refers to the position of an introduction agent and at 1.019 to canvassing or introducing agents. This is the position of real estate agents or TWL's sub-agents acting on behalf of Monrad acting on behalf of Blue Chip. Dal Pont *Law of Agency* (Butterworths, Australia, 2001) at 1.2.4 reinforces the limit of the mandate of real estate agents. In the common solicitor situation knowledge should clearly be imputed (*Burmeister v O'Brien* [2008] 3 NZLR 842 (HC); *Niak v MacDonald* [2001] 3 NZLR 334 (CA) and *Waller v Davies* [2005] 3 NZLR 814 (HC)).

The test for tainting is not in dispute. The sale and purchase agreements did not have the purpose or object of assisting a financial package but simply of conveying title. In *Portland*, the illegality was in the past, but that is irrelevant. What matters is knowledge of illegality; the question is whether you need knowledge of the law or just of the facts which create the illegality. Portland says that there must be knowledge of the law. McCarthy J in *Portland* was supported by North P. Turner J was equivocal. If the contract is illegal, the parties are caught. In *Allen v Cloke* there was common design, so it did not matter that parties did not know it was illegal, it was not a tainting case. Lord Denning drew a distinction with, for example, the laundry that cleans a prostitute's clothes, charging the usual price in the usual course of trade. There is no tainting in that case. In *Central Trust Co v Rafuse* (1983) 147 DLR 260 a loan was unenforceable, the lender sued solicitors for negligent advice. The solicitors tried to argue that their contract of retainer was tainted and unenforceable. There was no suggestion that the parties would have gone ahead if they had known it was illegal. Tainting of contracts affects banks, financiers. One is not normally required to inquire into the actions of other parties; there cannot be a duty to check that other parties to contracts are acting legally. Our first position is that the common law of tainting should not apply when statute creates a code and remedies. Tainting cases referred to by the appellants predate the 2004 amendments. This argument and the argument that the sale and purchase agreement is part of the allotment are new arguments; they were not raised below. [Reference also made in printed case to: *Petersen v Maloney* (1951) 84 CLR 91; *McAlpine Snowline v Wethey* (1986) 2 NZCPR 388 (HC); *Saunders v Leonard* (1976) 1 BPR 9409; *Lloyd v Grace, Smith and Co*; *Wyllie v Pollen* (1863) 3 De GJ & S 596; *Blackbury, Low v Vigors* (1867) 12 App Cas 531; *Sargent v ASL Developments* (1974) 131 CLR 634; *Martindale v Falkner* (1846) 135 ER 1124; *Kiriri Cotton Co Ltd v Dewani* [1960] AC 192 (PC); *Abbott v UDC*; *DFC v Abel*; *Spector v Ageda* [1973] 1 Ch 30; *Rooks Rider v Steel* [1994] 1 WLR 818; *Ostrowski v Palmer* [2004] HCA 30, (2004) 218 CLR 493; *Farrow Mortgage Services v Edgar* (1993) 114 ALR 1.]

O'Callahan for Icon: It is common ground that the sale and purchase agreements are not securities. It is the allotment of the security which is invalidated by s 37(4). Section 37(5) and (6) refer to further consequences of invalidity, including repayment of the subscription and interest. The investors received an option fee and if the option was exercised they received reimbursement of the deposit and expenses. The subscription is argued by the appellants to be the granting of the option by the investor. The obligation is therefore to undo the grant of the option. This demonstrates the limited nature of the concept of allotment and the obscurity of the way that the securities were said to arise. It is obscure to say that the grant of the option is the subscription. The 2004 amendments were not before the courts in *DFC Financial Services Ltd v Abel*, *Abbott v UDC Finance* or *Re AIC Merchant Finance*. The court can make relief orders on the conditions for compensation, and so on. Section 37AG empowers the court to order compensation for losses from contravention although continuing to hold the security. Under s 37AJ, the court can make other orders imposing terms and conditions the court does see fit. This does not plainly provide for orders in proceedings brought by third parties. Icon was not a "promoter"; knowledge that someone else is going to use your development for a security transaction is not sufficient. This idea has never been raised before and might require new evidence. Promoters are not mentioned in s 37; the remedies are aimed at issuers and at curing the problem faced in *Hurst v Vestcorp* that the statute did not lay down civil responses. The Court had to base remedies on illegality. Promoters can be liable for misleading prospectuses but where there is no prospectus they have not put their names to a misleading statement. Allotment is a matter of contract and there cannot be some integrated scheme outside the contract. No case has been found which incorporates into a scheme something not contracted for. The notion of an "integrated scheme" comes from *Hurst v Vestcorp*. The allotment in some cases is acceptance by a company of a registering subscriber for a debt security. In other cases, the allotment is the particular contractual covenant which gives rise to the security. There must be a contractual relationship between issuer and subscriber. In this case, it is the PIP agreement which contains the covenants which are the allotment. If there are invalidated, this does not affect the sale and purchase agreements. One would have to argue that the sale and purchase agreements are in some way conditional upon or are part of an "integrated scheme" with the financing arrangement. The Courts below found that the sale and purchase agreements were not conditional on the financial packages. The authorities are all consistent with the proposition that a contractual link is require. *Hurst v Vestcorp* concerned a film partnership promoted by FilmCo which offered loans to assist investors to participate. It marketed the loans at the same time and it was part of the consideration for granting the loans that the borrowers participated in the film investment (see 318). There were other interconnectors as well. The loan agreement recited that the borrower was investing in films and that the revenue from the films was to be paid to the lender until the loan had been paid off. No question of severance arises in this case, as there is no contractual dependence (see CA at [358]). One cannot apply dicta from cases involving severance. There is no implied term that a loan depends on the legality of the investment the borrower is going to make. There are a number of possible reasons for excluding land, but no particular authorities. Possible rationales are that an interest in land is not a security unless shared; or that land transactions commonly involve solicitors. The latter applies in this case as all the sales were off the plans; s 225 of the Resource Management Act 1990 implies conditions into an agreement which protect the purchaser. In *Culverden*, there was only a right to occupy in substance plus the contributory scheme. The exemption means that s 37 cannot avoid the property transaction part of a security transaction. The argument that the deposit was paid on behalf of Blue Chip is met by two arguments: first, it is paid by the purchaser as a stake for the vendor; second, if the deposit is the subscription then one must be driven to the land exemptions. There was no suggestion in the Courts below that the knowledge Icon had had any impact on the contractual relationship so the only issue is tainting. Icon did not know that these transactions were illegal.

Campbell, replying: Venning J found as a fact that TWL was aware that the apartments were to be sold in conjunction with the Blue Chip product (at [94], [100] and [106]). The extent to which it knew the detail is considered at [123]–[130]. TWL did not challenge these findings in the Court of Appeal and did not give notice that it would do so in this Court. With extraneous materials, the Act demands a substance over form approach. The Act refers to the right to be paid money, not to interest. The Court can look at extraneous documents under the ordinary law of contractual interpretation. Even if it were right that participation is necessary for there to be a debt security, there it as much a right to participate here as in any other situation. "Security" is so widely defined that it would capture offers of the sale of land, boats, and so on but s 5 says that Part 2 does not apply to them. *Culverden* was rightly decided and has been acted on ever since. The entire allotment has to comply with the Act and the allotment was entry into the sale and purchase agreement which had to be entered into prior to entering into the joint venture agreement. *Culverden* never refers to a licence to occupy, but to the right to occupy which came from an estate or interest in land. TWL's awareness in general terms as to the nature of the transactions means that it had the chance to protect itself by telling the agents not to sell financial packages. Watts' comments on Handley J's judgment are prefaced with "where the agent is entrusted with the contracting process".

Barter replied.

MINUTE OF THE COURT 27 April 2012:

[1] The Court is currently of the view that (a) the marketing by Blue Chip of its products involved offers of securities to the public which were not within the s 5(1)(b) exemption and (b) it must therefore address the question whether this conclusion affects the enforceability of the sale and purchase agreements.

[2] A possible route to a conclusion in favour of the investors would be as follows:

(a) in consideration for the allotment by Blue Chip of the securities it offered, the investors entered into sale and purchase agreements with the developers;

(b) for the purposes of s 37(5), the subscriptions made by the investors thus included their commitments and payments to the developers;

(c) because the developers received money and money's worth from the investors provided as part of their subscriptions for the securities, the developers are "issuers" in relation to those securities; and

(d) the practical effect of s 37(5) is that the developers must therefore refund any money received and are precluded from otherwise enforcing the sale and purchase agreements except pursuant to such relief as may be granted under s 37AH.

Amongst the questions which this line of argument raises are whether there can be more than one issuer in relation to securities and, if so, whether an issuer can be someone other than the offeror of the securities. No doubt there are others.

[3] This line of argument differs from that advanced by Mr Campbell at the hearing in that he did not seek to categorise the developers as issuers. Such a categorisation would mean that if the Court finds in favour of the investors, the developers would have scope to apply for relief under s 37AH, a section which might not necessarily be engaged if the Court were to find in favour of the investors on other grounds.

[4] The points on which we wish to receive submissions are:

(a) whether there would be any injustice to either appellants or respondents if we were to address the case in terms of this argument; and
(b) whether the argument is sound.

Dale (by memo 29 May 2012): entry into the sale and purchase agreements with the developers and the payment of the deposits to the developers was part of the benefit provided by the investors to Blue Chip in exchange for the allotment of other securities, and therefore part of the consideration for the allotments. "Subscriptions" in s 37(5) means money or other consideration received for the securities. This is also how it is interpreted in ss 36A, 38F(9)(b) and 44(6)(b) (now repealed) and in the new ss 4(b), 43F(2)(b) and 43G(3(b) (see also *Christchurch Pavilion Partnership No 1 v Deloitte and Touche Tohmatsu Trustee Co Ltd* [2002] UKPC 4, [2002] 3 NZLR 289 at [20]). In this case, the subscriptions therefore included the investors' entry into the SPAs which included their commitments to the developers and their payment of the deposits. The developers received this consideration and are therefore issuers in relation to those securities. This means that there are two issuers in relation to the securities, one of whom was not the offeror. This is compatible with the scheme of the Act which is to cast the net in the widest terms and then rely on exclusions to limit its scope. The Act is also concerned with the substance of transactions, not their form. If more than one party receives parts of the consideration, it would be odd if only one were regarded as an issuer. Usually the issuer will be the offeror, but there is nothing in the Act providing that this must be so and there are provisions which assume that the offeror is someone other than the issuer (ss 3(1)(c), (2)(a)(i) and (8) and 33). In ordinary language, an issuer is someone who grants the rights that constitute the securities, but the Act does not define "issuer" that way but focuses only on the receipt of consideration. The developers must repay the subscriptions to the investors, including in respect of the non-cash consideration. Where these include commitments, return is by release from the commitments. Section 37(4) does not operate on the SPAs as they are part of the allotment. It invalidates the allotment regardless of whether the allotter was also an issuer. Section 37(5) operates only on the issuer and ensures that if the allotment is invalidated, the consideration is returned to the investor.

Barter by memo (30 May 2012): The security was the lease included in the terms of the SPA. The offering of this security was "on behalf of", "in the interests of" and "for the benefit of" the developers and hence the developers were within the definition of issuer.

Neutze by memo (19 June 2012): the developer was not a party to the subscription contract and received no consideration under that contract. It cannot be an issuer. In consideration for the allotment of the securities, the investor agreed that it would assume responsibility for borrowings and make a payment to the joint venture company. It was no part of the JVA that the investor enter into the SPA with the developer. What was agreed was that the joint venture company would be the purchaser and that if the investor had entered into the SPA, that it nominate the joint venture company to settle the transaction. Entry into the SPA preceded entry into the JVA and the allotment of the securities and hence would be "past consideration" and hence not consideration (*Roscorla v Thomas* (1842) 3 QB 234 at 237). The subscriptions by the investors did not therefore include their commitments and payments to the developers. In *Christchurch Pavilion*, Lord Scott said that in s 37(5) "subscriptions" meant "money that has been paid" (at [20]). It has never been part of the appellants' argument that subscriptions included "commitments and payments to the developer". The section contemplates that the subscription moneys must be paid by the investor to the issuer and that the debt security comprises a promise to repay. Only a party to a contract may enforce it and if a party is to enforce a contract, consideration must have been given to it by the promisor (*Dunlop Pneumatic Tyre Co v Selfridge* [1915] AC 847 (HL) at 853). In the present case the developer is not a party to the joint venture agreement and did not receive the benefit of any enforceable promise made in the joint venture agreement by the investor. The developer makes no promise to the investor in the joint venture agreement. The solicitors for the developers received the deposits paid by the investors under the SPAs (not the JVA), but they were received by the solicitors as stakeholders on the trusts set out in the SPA, not as agents for the developers. The deposits were to be returned by the stakeholder to the purchaser if the SPA did not become unconditional (cl 16.2). The developer was not a party to the JVA and had no knowledge of the detail of the JVA. The appellants argue that the securities were the promises made by BCJVL to the investor. The liable party was hence BCJVL and the promises were the investors. The allotment was the assumption by BCJVL of the obligations under those promises. The consideration were the promises to assume all obligations and responsibilities for the borrowings of the joint venture and to provide the initial contribution to the joint venture company. The consideration was provided by the investors to BCJVL. Even if consideration is given an extended meaning, the recipient is still BCJVL as it was the party that requested the acts of contractual performance and for whose benefit they were done. In neither case was the consideration a payment to the developer. Equivalent arguments apply to the PIP contracts.

It is possible for there to be more than one issuer, but for this to be the case, each of the co-issuers must undertake jointly to the lender in the same terms (see s 86(1) of the Bills of Exchange Act 1908). The developer was not a party to the JVA or PIP and did not undertake any joint obligation with BCJVL or BCPI in respect of Blue Chip's obligations under the alleged securities. The offer of a security must be made by on behalf of the issuer (s 33(1)). Taking into account the definition of "issuer" in s 2, and ss 33 and 37 in particular, "the person on whose behalf any money paid in consideration for the allotment of the security is received" must be the person by or on whose behalf the offer was originally made, who is liable on the contract of subscription to the investor, who receives the investor's counter-promise to pay the subscription moneys and who allots or procures the allotment of the security.

Greenstone Barclay would be prejudiced by the new and unpleaded argument and adopts the submissions of TWL on this point. [Reference also made to: *Thomas v Thomas* (1842) 2 QB 851; *Hill v Haines* [2007] EWCA Civ 1284, [2008] Ch 412; *Bolton v Madden* (1873) LR 9 QB 55; *Fibrosa Spolka Akeyyjna v Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, [1942] All ER 122 (HL).]

Chisholm by memo (18 June 2012): TWL adopts the submissions of Greenstone Barclay. The Act does not provide exclusions from the definition of "issuer" and so care must be exercised in giving the term a wide definition. It should not be extended to a non party to the offer or allotment who received a benefit or a potential benefit under a related agreement. TWL was not a party to and did not know of the terms of the Blue Chip agreements. On the face of the PIP and JVA agreements, the investors did not enter into the sale and purchase agreements in consideration for entering into the Blue Chip agreements. If the definition is extended in this way, lenders funding an investment as in *DFC Financial Services v Abel* or *Abbott v UDC Finance Ltd* would be issuers, along with the parties mentioned by the Court of Appeal at [301]. There would be bizarre consequences under ss 33, 37(5) and (6), 51–54C and 59 of the Securities Act. Third parties would be required to determine whether other parties were complying with their statutory obligations. The Act was not intended to make entities that had no knowledge of the allotment issuers.

This argument has not been pleaded. A second appellate court should only rarely and with extreme caution allow a point to be raised that had been conceded below and should not do so if there is any possibility that the outcome might have been affected had the point been taken earlier. The Court needs to be persuaded beyond doubt that it has all the evidence it requires to decide the point (*Otago Station Estates Ltd v Parker* [2005] NZSC 16, [2005] 2 NZLR 734 at [11] and [12]). Pleadings are binding on the parties (*Esso Petroleum Co Ltd v Southport Corporation* [1956] AC 218 (HL)) and judges should not "enter the fray": *Ye v Minister of Immigration* [2008] NZCA 291, [2009] 2 NZLR 596 at [355].

O'Callahan by memo (19 June 2012): On the evidence, in the PIP cases concerning Icon, the SPAs were entered into prior to the PIP being concluded. Entering into the SPA cannot therefore have been consideration for entering into the PIP. Any suggestion that the PIP was dependent upon the SPA was rejected in the Courts below and not reopened by the appeal to this Court. It cannot be argued that if the PIPs had not been executed, the SPAs would have fallen away. In the PAC cases, the deed recites that the SPAs had already been entered into and this raises estoppel by deed between the parties. The parties treated the SPAs as executed and entry into the SPAs cannot therefore be consideration for entry into the PACs. There was also evidence that the SPAs were delivered to the purchasers, signed by Icon. The Court's proposed argument would lead to a company which was not a party to the agreements that contained the securities and did not know about them being an "issuer" in respect of the offer and allotment of securities. This cannot be correct. It cannot have been intended that the Securities Act makes an issuer of someone who is not a party to the contract of subscription. Icon was not a party and what it knew or did not know is hence irrelevant. The Herricks have argued that the lease is a security. No leave was given to make this submission and the Court should not take it into account. The Herricks also allege that Icon was the issuer of the SPA and its associated lease. If that is the allegation, s 5(1)(b) clearly applies.

Cur adv vult

Reasons

The reasons of Elias CJ, McGrath, William Young and Anderson JJ were given by

WILLIAM YOUNG J.

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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 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).

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

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

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);
- 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

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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.

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.

[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

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.

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 10 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

10 Now called 74 Albert St Ltd.

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 $39m 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 $20m, 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.

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

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

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.

[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 $73m) 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:

> **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.

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.

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

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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].

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.

> 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 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 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

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

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 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]

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19 *Australian Softwood Forests Pty Ltd v Attorney-General (NSW); ex rel Corporate Affairs Commission* (1981) 148 CLR 121.
20 Now repealed.
21 *Culverden Retirement Village v Registrar of Companies* (1996) 1 BCSLR 162 (CA); affirmed [1997] 1 NZLR 257 (PC).
22 At 165–166.

> 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 s 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 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

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23 At 260.

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 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 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.

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).

[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.

25 Five per cent in the case of the JVAs.

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 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 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:

26 See [112] and following.

> 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 Part 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; —

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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).

> 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 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 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.

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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).

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 ofan 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 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.

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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.

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 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.

[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

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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].

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

39 At [137]–[140].

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.

[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

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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].

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

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.

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

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44 At 46.
45 *Morgans v Launchbury* [1973] AC 127 (HL) at 135.
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.

> 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 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, *Nathan v Dollars & Sense Finance Ltd*.[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

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

> 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. 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 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

51 Above ns 36–37.

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 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.

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

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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.

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].

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.

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:

> (5) 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:

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.

(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.

[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

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.

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.

[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

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58 See Securities Act 1978, s 6.
59 See [12] above.

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 –** (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;
(b) and 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.

60 The relevant sections were inserted in the Act by s 12 of the Securities Amendment Act

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.
(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

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.

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

consideration provided by the subscriber. In present 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.

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,

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

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 illegaland 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.

[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

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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).

66 MP 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, Wellington, 2012) 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.

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 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.

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).
73 At 221.

[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 it 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 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

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74 At 223–224.
75 At 228.
76 *Scott v Brown, Doering, McNab & Co* [1892] 2 QB 724 (CA).
77 At 728.
78 See definition of offence in s 2(1) of the Crimes Act 1961.

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 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.

[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

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

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 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

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

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 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?

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 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.

[154] 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

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

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.

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?

[155] 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?

[156] 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.

[157] 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*

[158] 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]

[159] 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

86 At 583.

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]

> 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.

[160] 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

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

Orders

(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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87 At 581.
88 At 597.

(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.

Appeal allowed.

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Solicitors for Turn and Wave Ltd: *CMS Legal* (Auckland).
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Reported by: Bernard Robertson, *Barrister*