Preliminary paper No 16

THE PROPERTY LAW ACT 1952

A discussion paper

The Law Commission welcomes your comments
on this paper and
seeks your response to the questions raised.

These should be forwarded to:

The Director, Law Commission, PO Box 2590,
Wellington

by Friday 1 November 1991

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* Those statutes noted with an asterix are New Zealand law by operation of the Imperial Laws Application Act 1988.

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PART A: INTRODUCTION

I
THE PROPERTY LAW ACT 1952

NATURE AND HISTORY OF THE ACT

1 The Property Law Act 1952 contains a collection of miscellaneous rules relating to property of all kinds, including land. It is not a code, more a repository for legislative supplements to or corrections of judge-made law. Where it has been thought that the rules of common law or equity have fallen short of producing a sensible solution to a problem concerning the creation, disposition or control of property interests, legislative attention has been given to the problem by way of a section in the Property Law Act or one of its predecessors.

2 While the Act has been the subject of much addition and amendment relating to individual topics, and has been consolidated in 1883, 1905 and 1952, it is fair to say that there has been no general review, overhaul and reformulation of its content since the original Conveyancing Ordinance of 1842 which is said to have been drawn up by Sir William Martin and William Swainson during their voyage from England to New Zealand.

3 The Conveyancing Ordinance was for its time, and in its circumstances, a remarkable achievement. It began:

> Whereas by the law of England there are various forms of assurance for the transfer of property and divers rules relating thereto which by lapse of time have become inconvenient and are altogether unsuitable to the circumstances of this Colony; for the simplifying and amending thereof - Be It Enacted ...

It consisted of 56 sections. It laid down rules concerning the formalities and operation of deeds (which were in those days of more importance than they are now). It set out forms of covenants to be implied in deeds, including leases, and not a few of the rules contained in Part II of the present statute are found in their original form in the 1842 Ordinance.

4 An amendment in 1860 introduced mortgagee sales for real property through the Registrar of the Supreme (now High) Court. The mortgagee was given the right to become the purchaser at such a sale. In 1870 the Partition Act copied English legislation of 1868 enabling a court to make an order for sale of land in lieu of partition. (Only in 1952 was the court empowered to make orders in respect of jointly owned chattels.)

5 The Supreme Court Act 1882 made relief against forfeiture of leases available to supplement the equitable jurisdiction of the court but that provision was not carried over into the Property Law Act when the first of the consolidating measures, the Property Law Consolidation Act,

was passed in the next year. The Property Law Consolidation Act repealed the Conveyancing Ordinance 1842 and the other Acts which have been mentioned, apart from the Supreme Court Act. But it added little new material of relevance today. The consolidation process expanded the new Act to 98 sections.

6 Over the next 20 years property statutes of note enacted by the New Zealand Parliament were the Apportionment Act 1886 and the Light and Air Act 1894 (both of which were moved into the Property Law Act in the 1908 general consolidation), and the Mortgages of Land Act 1901 which enacted a set of implied covenants in mortgages - the predecessor of the optional covenants, conditions and powers for mortgages of land found in the Fourth Schedule of the 1952 Act.

7 The Property Law Act 1905 (122 sections) was another consolidating statute. Some new sections were also inserted, including provisions for the creation of easements in gross, the execution of deeds by corporations, the running of the benefit and burden of covenants in leases, a prohibition on the taking of a fine for consent to an assignment of a lease and specification of the manner in which notices under the Act should be served. The 1905 Act contained provisions relating to mortgages, including the requirement that a mortgagee should not call up the principal amount where the mortgage was running on overdue without giving three months' notice of intention so to do (the present section 90). The implied covenants by tenants were also varied. In particular the obligation to pay rent was qualified in respect of fair wear and tear and destruction or damage caused by fire and some other perils. The provisions relating to relief against forfeiture sections (now within the Act) began to assume their modern form. The Statute of Uses was repealed.

8 There was surprisingly little reform of basic property law outside the Land Transfer legislation between 1905 and 1952. Few changes were made in the general consolidation of the statute book in 1908. An amendment to the Property Law Act in 1927 added the present sections 124 and 125 relating to light and air easements. A year later came the sections enabling a lessee to have relief against the lessor's refusal to grant a renewal or to convey the reversion (under sections 120 and 121). In 1936 covenants against assigning, under-letting or parting with possession of leased premises were deemed to be subject to a proviso that consent be not unreasonably withheld (now section 110). In 1939 the well-known provision requiring a mortgagee to give formal notice before exercising a power of sale, or entering into possession or using an acceleration clause (now section 92) came into the Act and in 1950 the court was empowered to authorise entry on neighbouring land for the purpose of erecting or repairing a building, wall, fence or other structure on the applicant's land. There has also been from that time a section (now section 129) enabling the grant of relief in the case of encroachment.

9 However, there was no attempt in New Zealand to match the fundamental reforms achieved in England by the Law of Property Act 1925. This was because few of the reforms in that Act were necessary in New Zealand since many of them related to forms of tenure which have never been known in this country, and also a good deal of the other work had already been done in the pioneering Conveyancing Ordinance of 1842.

10 In New Zealand the Property Law Act is not the fundamental landholding statute. That was and remains the Land Transfer Act. There had for some years been doubts expressed concerning the manner in which the two statutes should operate alongside each other. Some work had apparently been done on this subject before World War II but it was not until a personal initiative by the Hon H G R Mason KC that any legislative attempt was made to rationalise the operation of the two statutes. The result was the Property Law Amendment Act 1951 which passed through Parliament and was to come into force on 1 January 1953. A large part of that Act was designed to achieve a correlation between the Property Law Act and the Land Transfer Act but some ideas were also taken from the 1925 legislation in the United Kingdom.

11 Events caught up with the 1951 amendment. Before it could come into force it was repealed by a new statute, the Property Law Act 1952, which remains in force and is the subject of this present review by the Law Commission. When it was passed, it consisted of 155 sections. It was for the most part merely a consolidation although there were several notable reforms: abolition of estates tail, which were already obsolete in practical terms in New Zealand (section 16); the enabling of registration of restrictive covenants under the Land Transfer Act; extension of the relief against forfeiture sections to the interests of purchasers in possession under agreements for sale and purchase (section 50); and a section making a person acquiring land already subject to a mortgage ipso facto personally liable to the mortgagee (section 104).

12 The changes intended to be made in the 1951 amendment were incorporated in the 1952 legislation. (For an account of the intentions of those responsible for the consolidating Act see H G R Mason KC's article in [1952] NZLJ 24 and the series of commentaries by E C Adams in [1953] NZLJ 25, 41, 56, 90, 106, 121, 137, 155 and 168.)

13 There have been 16 Property Law Amendment Acts since the original 1952 statute. The most significant amendments in force are:

- section 80A (contractual tacking) added in 1959, with amendment in 1975;
- section 129A (relief in cases of mistake as to boundaries or identity of land) added in 1967;
- section 33A (voiding provisions in connection with disposition of property imposing

restrictions on grounds of colour, race, ethnic or national origins) inserted in 1965;

- section 66A (enabling covenants and agreements to be made by a person with himself) in 1968;

- sections 104A-F, 107A and 107B and 116A-M (rules relating to leases of dwelling-houses) inserted in 1975 but largely replaced by the Residential Tenancies Act 1986;

- sections 129B and 129C (dealing with landlocked land and trees or structures on neighbouring land) in 1975;

- section 49A (formalities for the creation of interests in land, substituted for portions of the Statute of Frauds) added in 1980 but amended in 1982;

- section 80B (enabling a mortgagor to sue a mortgagee without first offering to redeem) in 1982;

- amendments to the notice provisions of section 92 and to section 152 (dealing with the service of notices) in 1982; and

- sections 64A, 126 and 126A-G (enabling the running and notification on the Land Transfer register of positive covenants and implying rights in easements of vehicular right of way) in 1986.

14 While the importance of many of the amendments which have been made to the 1952 Act is beyond doubt, the body of rules which it contains has not been the subject of any thoroughgoing review since the original Conveyancing Ordinance of 1842; nor, apart from work done on the Queensland Property Law Act 1974-1986, does any such general review appear to have been carried out in England or elsewhere in Australasia in the last 60 years. As a consequence of this and of the piecemeal introduction of new material the present Act is drafted in a variety of styles, none of which would evoke much enthusiasm in a modern drafter, and contains much that is obscure in its language or can be justified, if at all, only by its historical origins.

DEEDS SYSTEM LAND

15 When the last consolidation occurred it was still a relatively common experience to encounter land which remained under the deeds system, although for all practical purposes once such land was discovered it had to be brought under the Land Transfer Act in order to be dealt with. But to protect the position of those interested in deeds land, the 1952 Act brought forward a number of sections expressed not to apply to

land transfer land (see the First Schedule which refers to 15 sections or nearly 10 per cent of the original 1952 statute). Since then deeds land has all but disappeared. Any parcels are small and unlikely to be of much importance. It is almost inconceivable that anyone will knowingly try to convey or mortgage them without first bringing them within the Land Transfer Act. It is therefore tempting to suggest that the sections simply be repealed. However, to guard against the (theoretical) possibility that they may be needed in some unexpected situation we suggest retaining the sections, despite repeal of the 1952 Act, but without repeating them in the new statute. The new Act could provide simply that in the case of deeds system land the sections in question in the 1952 Act should continue to apply.

Question:

Q1 Should the deeds system sections be preserved?

RELATIONSHIP WITH LAND TRANSFER ACT

16 The rationalisation of the respective functions of the Property Law Act and the Land Transfer Act was very successful. However, the Law Commission believes that some residual work has yet to be done in this area: it should be made abundantly clear that the new Property Law Act, with which we suggest the present Act should be replaced, applies to both registered and unregistered interests in land which is under the Land Transfer Act but that, unless there is an express statement to the contrary, the Property Law Act is to be subordinate to the Land Transfer Act. Where there is any conflict between the rules found in the Property Law Act and the principles of the Land Transfer system, the latter should, as at present, prevail (see section 3 of the Property Law Act and its converse, section 244 of the Land Transfer Act).

MOVEMENT OF RULES

17 There are a few sections in the Land Transfer Act which are of general significance; these should apply regardless of whether registration has taken place. It is suggested that sections 96, 98, 104, 106 and 108-110 therefore be transferred to the Property Law Act. Sections 96 and 98 respectively deal with the obligations of those who take title subject to an existing mortgage or who acquire leasehold interests. The other sections concern the rights and obligations of mortgagees. All should certainly apply when the interest in question is registered but, equally, ought to apply to unregistered interests.

18 The Law Commission has concluded that any review of the Property Law Act should encompass the Contracts Enforcement Act 1956 and should *either* bring the provisions of that Act within a new Property Law Act (which is where comparable provisions are found in England and Australia) *or* should

introduce an entirely new rule concerning the need for a writing in relation to the creation or transfer of any interest in land, as has been done in England by section 2 of the Law of Property (Miscellaneous Provisions) Act 1989 (see paras 101 to 123).

19 In contrast, the Property Law Act contains two sections (sections 131 and 132) dealing with the powers of trustees under marriage settlements. Even leaving aside the fact that marriage settlements of the old style are now uncommon, the sections seem out of place in a general property statute and, to the limited extent that they go beyond the provisions of the Trustee Act 1956, they would be better preserved within that Act (see para 649).

OTHER DEFICIENCIES OF THE ACT

20 Some of the other deficiencies of the Property Law Act are briefly mentioned below. These deficiencies (and others) are to be redressed by the proposals for a new Act.

Language

21 Because of the origins of the Act, many sections are couched in ancient terminology. It is of importance that property law should be made more accessible. A new Act should modernise this language and replace expressions which have better understood equivalents (as has already been done in the case of residential tenancies by the Residential Tenancies Act 1986). An example is "re-entry and forfeiture" (section 118 of the Property Law Act) referring to the process of terminating or cancelling a lease for breach. A new statute could use the expression "termination", which means the same thing as cancellation but is more commonly used in referring to the cessation of a leasehold interest. The expression "re-enter" would, necessarily, continue to be used where the reference is to the physical act of the landlord entering upon the premises in order to terminate the lease. As a further example, it may be possible to delete "executory limitation" in section 23 and replace it with the more familiar "gift over". Where a section cannot be adapted to a more common description, as in the expression "contingent remainder" in section 20, a definition could be provided. Section 86 (sale of mortgaged property in redemption action) and sections 112-114 (running of lease covenants) are particularly bad examples of avoidable obscurity. A new statute will also need to use terminology consistent with the High Court Rules.

Mortgages

22 The present Act lacks a coherent pattern in its treatment of mortgages. It is not proposed to attempt the very large task of codification of the law of mortgages but the relevant sections need clarification and some amplification, particularly in relation to the rights and obligations of a mortgagee in possession. The restrictions on

a mortgagee's powers of sale and entry into possession and upon the use of acceleration clauses (the right to call up the principal in the event of default) require restatement in clear language. Anyone coming to section 92(1) for the first time is likely to struggle to ascertain quickly what it is that is prohibited before the expiry of a notice to the mortgagor.

23 Although implied covenants in mortgages or charges over personal property exist in the Chattels Transfer Act 1924, no rules or implied terms for such securities appear in the Property Law Act. If, as seems likely, the Chattels Transfer Act is to be replaced, there may be merit in recasting the implied conditions for both real and personal property and placing them alongside one another in Schedules to the proposed new Property Law Act.

24 As has been mentioned, section 92 of the Act places restrictions on the exercise of a mortgagee's rights in relation to land. But there is no such restriction on a mortgagee of chattels. Later in this paper we suggest that this should be considered (see paras 340 to 345).

Leases

25 Arguably, the most deficient area of the present Act relates to the law of landlord and tenant. The layout of Part VIII of the Act, since the insertion of sections dealing with dwelling-house leases in 1975, is very messy. The Law Commission suggests that these sections be removed to the Residential Tenancies Act 1986 or that the scope of that Act be extended so that they are no longer necessary (see para 617).

26 One of the present difficulties is that the definition of "lease" appears not to include an oral lease (which at the moment can be created for a term of up to three years as a legal lease) or a statutory tenancy under section 105 of the Act. It seems better to have the term defined in a manner which encompasses all leases, stating any exception in particular sections. We also propose adoption of the suggestion by the Property Law and Equity Reform Committee (PLERC) in their *Final Report on Legislation Relating to Landlord and Tenant* (1986) that the exception for an oral lease be reduced to a lease of one year or less including periodic tenancies. We record our debt of gratitude to that committee. Their report has made our task much easier in relation to the law of leases. We have very largely adopted their suggestions.

NEW PROPOSALS

27 The Law Commission's review of the Property Law Act has presented an opportunity to review the operation of certain rules of common law and equity pertaining to property, the object being to eliminate or reduce the effects of commercially unrealistic or inequitable rules.

28 Examples of suggestions for inclusion in a new Act are:

- equitable mortgagees to have power of sale of mortgagor's legal estate and court assistance to do so (para 269);
- warning notice to be given before mortgagee sale of personal property (paras 340 to 345);
- abolition of rule in *Hopkinson* v *Rolt* (para 362);
- assignor of lease to be guarantor of assignee rather than concurrently liable (para 451);
- lessee not to be liable for negligence causing destruction or damage to premises by fire or other peril where lessor has insurance cover (para 482);
- sublease for same or longer term than head lease to operate as sublease and not as assignment (para 493);
- controls on lessor's refusal of consent to a change of use of the premises (paras 510 to 519);
- lessee to have reasonable period after end of term for removal of trade and agricultural fixtures (para 596); and
- unlawful eviction from part of premises not to suspend the whole of the rent (para 601).

IMPERIAL STATUTES

29 All or part of twelve imperial statutes relating to property survive and are in force in New Zealand having been specified in the First Schedule to the Imperial Laws Application Act 1988, that legislation enacted following the Law Commission's Report No 1 *Imperial Legislation in Force in New Zealand*. The text of each of these imperial statutes can be found in that report. The Law Commission has reviewed them all. We detail later in this paper our proposals whereby each will be repealed and, where appropriate, replaced by a section in the new Act. Examples of those proposed to be entirely repealed are the old statutes relating to distress (including the Distress for Rent Act 1737). PLERC, after extensive consultations and submissions, concluded that there was little case for, or support of, retention of this medieval right of landlords and that its "self-help" remedy was inappropriate in modern law (para 569).

30 Another imperial statute of significance to the law of landlord and tenant is section 4 of the Landlord and Tenant Act 1730 which gives a tenant the right to bring to an end proceedings for forfeiture for non-payment of rent by

tendering all arrears and costs. But in this case the provisions of the English statute should, we think, be subsumed into a new section dealing with relief against forfeiture (para 549).

MAORI LAND AND CROWN LAND

31 In the preparation of the new statute it is necessary to consider the extent to which it should apply to Maori land and to Crown land. The present statute contains a statement in section 155(8) that any provision of the Maori Land Act 1931 (which has been replaced by the Maori Affairs Act 1953) or any other enactment relating to property that prevailed over the former Property Law Act prevailed over the 1952 Act. The 1952 Act applies to Maori land by virtue of the broad definition of "land" in section 2. Because the Property Law Act is of a general nature, it would in our view be subject to the provisions of the Maori Affairs Act 1953 and to any other specific legislation which may be in point regardless of section 155(8). There are two exceptions in relation to Maori land. When sections 129B and 129C were inserted in 1975 to deal with the problems of landlocked land or trees or structures injuriously affecting the land of a neighbour, both were expressed to apply to Maori land. In these particular cases, then, it seems that the Property Law Act is to override the Maori Affairs Act - but not otherwise. The Law Commission believes that, unless particular areas akin to those dealt with in sections 129B and 129C are identified, the present arrangement should not be disturbed.

32 It is best, we think, not to encumber a new Property Law Act with statements to the effect that it is to be read subject to other Acts (except the Land Transfer Act), relying instead upon the maxim *generalia specialibus non derogant*. Otherwise the omission of reference to a specific statute may lead to the conclusion that it is overridden by the Property Law Act. In the case of the Land Transfer Act, there is precedent in the legislation for an express statement. There might otherwise be doubt about the interrelationship of those two general Acts.

33 As for the Crown and its land, the Law Commission in Report No 17, *A New Interpretation Act*, has recommended that the Crown should in general be subject to statutes. It proposed that a new Interpretation Act should contain a provision stating that every enactment binds the Crown unless it otherwise provides or the context otherwise requires.

34 The 1952 Act is not expressed to bind the Crown. Indeed, from references in individual sections stating that those sections bind the Crown, it must be inferred that the balance of the Act does not. (See sections 13, 37A, 37B, 104B, 129B and 129C.) Most of these sections were inserted relatively recently. It is perhaps significant that when the legislature wished to deal with landlocked land and trees and structures injuriously affecting a neighbour's land, it found no difficulty in making the law on those matters apply to the

Crown. In 1975 all the provisions on leases of dwelling-houses were made binding on the Crown, as was the Residential Tenancies Act in 1986.

35 Given that specific statutes concerned with Crown land (such as the Land Act 1948) will in the normal way override the general provisions of the Property Law Act, we have tentatively concluded that all provisions of a new Act should bind the Crown. (If the new Interpretation Act proposed by the Law Commission is enacted, it will be unnecessary to make any such statement in the new Property Law Act.) We have, in coming to this conclusion, reviewed each of the provisions of the existing Act, and our proposals, to see if there would be anything unreasonable in the Crown being bound by them and have taken advice from lawyers with experience in representing the Crown in property matters. Nothing has emerged from these processes which suggests that difficulties are likely to be caused for the Crown. Nor have we detected good reason why the Crown should, for example, be beyond the reach of an application by its lessee for relief against forfeiture or be able to sell up its mortgagor without prior written notice which has been adequately served. We would be interested to receive comments on our proposal that a new Property Law Act should bind the Crown.

Questions:

Q2 Should the Property Law Act apply to Maori land?

Q3 Should the Property Law Act bind the Crown?

TERMINOLOGY

36 A glossary of technical expressions appears at 208. Readers of this paper should, in considering our proposals, assume that, unless the context requires, we make no distinction between:

- mortgages and charges (both registered and unregistered); or
- leases and tenancies ("landlord and tenant" being used interchangeably with "lessor and lessee").

37 All references to a lease, unless the context requires, include oral tenancies and statutory tenancies (of the kind now found in section 105 of the Act). "Tenancy" is commonly used for a short term occupation, particularly of residential premises (though the Residential Tenancies Act 1986 applies to "tenancies" for a fixed term of up to five years) but there is in law no hard and fast distinction between a lease and a tenancy.

38 References to "covenants" are not restricted to promises made by deed but include those made in informal documents. The implied covenants would apply, in the case of leases, to oral tenancies.

PROPOSALS

39 The Law Commission has engaged in considerable research and consultation in the preparation of this preliminary paper, but its conclusions are at this stage provisional. In most instances we have, however, thought it best to indicate clearly the direction in which we are leaning. To avoid further lengthening what is already a sizeable and sometimes technical paper we have in many cases omitted discussion of reforms which we do not favour. We have also omitted discussion of some matters of lesser importance or of detail which are not likely to be controversial. We are conscious of these omissions and would not wish readers to think that we intend to close off discussion of them. We are very aware of the possibility that those with a working knowledge of property law or engaged in teaching it may be in a position to make available to the Law Commission useful information about the operation of the present Act, or matters arising from the general law, which have not come to our notice. We would particularly like to hear about any existing practices adopted by conveyancing lawyers which might be adversely affected by any of our proposals.

40 In some instances where we have dealt fairly shortly with a particular matter, further research could be undertaken. However, we are doubtful that the Law Commission's resources can justifiably be used for that purpose: it might be interesting, but our present view is that it is unlikely to influence our ultimate recommendations in any substantial way.

41 The Law Commission welcomes any information on the operation of the law, together with examples, which may confirm our conclusions or lead us to consider a different solution. We hope also that readers may be able to suggest further reforms of the existing statute, especially matters which might be included for the first time.

ACKNOWLEDGMENTS

42 We are grateful to those who have already written to us concerning the Act. Their comments have been most helpful. We are particularly indebted for their assistance to our principal consultants, Professor Jock Brookfield and Dr Don McMorland, and to the following persons who have read and commented on some of our internal memoranda and drafts for legislation: Peter Barker, Professor John Burrows, Steven Dukeson, Roger Fenton, David Goddard, Professor George Hinde, Derek Levett, Rob McInnes, John Marshall, Frank Riley, Denis Sheard, Catherine Yates and Peter Young.

OUTLINE OF PAPER

43 The format of the balance of this preliminary paper is as follows:

Part B deals with general rules relating to property and contains chapters on:

- Formal requirements for execution of documents

- Reform of old property rules
- Agreements for sale and purchase
- Assignments of things in action
- Voidable alienation
- Covenants.

Part C discusses the law relating to mortgages and has chapters on:

- Mortgages of land
- Mortgages of personal property
- Mortgages of property generally
- Sales by mortgagees through the Registrar of the High Court.

Part D discusses the law relating to leases and has chapters on:

- Covenants in leases
- Lessee's liability for negligently damaging premises
- Subleases
- Restrictions on disposition or user of leased premises
- Breach of lease terms by lessee
- Miscellaneous reforms to law of leases
- Long-term dwelling-house leases.

Part E contains chapters dealing with further miscellaneous matters:

- Easements, covenants, encroachments, landlocked land, trees and structures
- Marriage settlements
- Service of notices
- Right to have insurance proceeds applied in reinstatement.

It will be observed that for the most part this format follows the sequence in the 1952 Act, but it should not be thought that the Commission is necessarily intending to recommend preservation of that sequence.

PART B: GENERAL RULES RELATING TO PROPERTY

II
FORMAL REQUIREMENTS FOR EXECUTION OF DOCUMENTS

DEEDS

Decline of importance

44 At common law execution of a deed by an individual or a corporation required the affixing of a seal. Sealing was a means of identification of the parties to the deed and authentication of their signatures. The importance of the deed in medieval times derived from the difficulty of proving facts to the satisfaction of the Royal courts. They developed stringent requirements of evidence, proof and form in order that the facts in issue could be established objectively. They permitted an action of covenant to enforce obligations; but only those obligations which had been stipulated in an instrument made under seal - a deed (Baker at 265).

45 It was found that the action of covenant had many inconvenient features. By the middle of the fourteenth century the Courts had accordingly begun to recognise a form of action called originally "trespass on the case" and later "assumpsit". It was the origin of the modern law of contract. In the words of the British Columbia Law Commission's Report on *Deeds and Seals* (1988):

> The decline of covenant was swift. It was supplanted by assumpsit. It continues, however, as cause of action separate and distinct from contract. (at 7)

46 So the action of covenant still survives and is the means by which a deed is enforced.

47 Twenty-one years ago, the law relating to deeds in New Zealand was comprehensively reviewed in an article under that name (J F Burrows (1970) 2 *Otago Law Review* 240). Professor Burrows concluded that a deed is in New Zealand no longer the all important legal document that it used to be:

> There are a few cases where it remains necessary to effect a conveyance or perform a legal act, but, mainly as the result of statute, lesser documents are sufficient to accomplish many conveyancing transactions. More than that, as a result of the intervention of equity, sometimes even where a deed is strictly required by statute a document not in the form of a deed may nevertheless have substantial legal effect. (at 260)

48 He pointed to a few situations where, at the time of writing, a contract still had to be by deed. Some of those have since disappeared, as has the need to stamp a deed with deed duty.

49 Leaving aside the very rare situation in which land under the deeds system has to be conveyed, conveyancing transactions are either carried through by documents intended to be registered under the Land Transfer Act (in which case the form is prescribed by the Act) or are executed in the form of deeds. Nevertheless, in the case of the conveyancing of unregistered interests in land transfer land for valuable consideration the modern development of the law of equity has resulted in there being little (if any) significance in whether the conveyance is a deed or a mere writing which falls short of constituting a deed. Equity will enforce the latter and, in either case, the only way in which the right of the grantee to a legal interest in land can be created is by order of the court that a document in registrable form be executed and registered. (A lease for less than three years is an exception to the usual rules: it can be created as a *legal* interest even orally.)

Use of deed

50 Professor Burrows identifies some particular instances in which a statutory provision requires documentation of a transaction in a deed:

- disclaimer of an interest in land (section 12 of the Property Law Act);
- disclaimer of a succession interest by a person entitled to a share in an estate on an intestacy (section 81 of the Administration Act 1969);
- disclaimer of a power (section 34 of the Property Law Act); and
- an approved compromise with creditors by a bankrupt (section 123 of the Insolvency Act 1967).

51 Burrows also observes that a deed is sometimes necessary for a person to achieve a new status. A trustee must retire by deed (section 45 of the Trustee Act 1956) and a new one appointed similarly (section 34 of the same Act). A guardian of children can be appointed extra-judicially only by deed or will (section 7 of the Guardianship Act 1968).

52 There is also the deed poll by which a person can change his or her name. A power of attorney to execute a deed must also be created by deed.

53 Burrows comments that "the legislature seems to have realised that there is more point in clarity and uniformity than in blind adherence to the format of the deed" (at 246).

54 The most important advantage of the use of a deed which still survives would seem to be the rule that although a promise made without consideration is unenforceable as a mere contract, since consideration remains an essential element in the formation of a contract, such a promise is legally binding if contained in a deed. The promise in the deed is being

enforced in covenant rather than in contract. Covenant developed before the concept of consideration, the courts in the thirteenth and fourteenth centuries being prepared to enforce promises of which there was sufficient evidence regardless of the absence of consideration. The fact that the primary function originally performed by deeds was evidentiary was later forgotten.

Limitation period

55 The other significant advantage in the use of a deed is that the limitation period where enforcement of its covenants is sought is 12 years, as opposed to six years in the case of breach of contract. (See, however, the Law Commission's proposed reform of the Limitation Act 1950, which, if adopted, would abolish this distinction: Report No 6.)

Possible reforms

56 Section 4 of the Property Law Act (which has its origin in sections 1 to 3 of the Conveyancing Ordinance 1842) modifies the common law relating to deeds, dispensing with sealing (for individuals), formal delivery and indenting. A choice is available between two paths for reform in the law relating to deeds in New Zealand. The first would involve minor adjustments to the present section 4, which has already substantially relaxed the formalities required for a deed: in New Zealand it is already unnecessary for a deed to be sealed by an individual or to be formally delivered, though delivery must still occur, in the sense that it must be seen from the circumstances that the party sought to be bound by the deed did intend to be bound. It must also be shown that any condition precedent to the operation of the deed - an escrow - has been satisfied.

57 The second possibility is to dispense altogether with deeds, leaving the formalities of conveyancing and other transactions to be specified in particular statutes, such as the Land Transfer Act 1952.

Modifications to section 4

58 We turn now to the first of these possible approaches. Minor modifications which could usefully be made to section 4 are:

- Adoption of the proposal of the Law Commission in England in its report on *Deeds and Escrows* (Law Com 163, 1987) that the rule of law which restricts the substances on which a deed may be written be abolished.

- Adoption of their suggestion that any rule of law which requires that the authority by one person to another to deliver an instrument as a deed on the first person's behalf be itself given by deed, be abolished.

- Inclusion of a statement that the witness to each signature must - except in the case of a corporation - be someone who is not a party to the deed (see *Mostyn v Mostyn* (1991) ANZ Conv R 100).

- Clarification of section 4(3) which presently provides that:

> Formal delivery and indenting are not necessary in any case.

This might suggest that *any* requirement for delivery had been abolished but the emphasis is on the word "formal". As Professor Burrows puts it:

> Delivery, in other words, is now nothing more than a synonym for the party's intention to be bound. (at 243)

His views on this point were accepted by the High Court in *Re Borley Holdings Ltd* (1987) 2 BCR 407.

It could be spelled out that a deed does not obtain operative status until there has been delivery in this sense. Care would have to be taken to preserve the law of escrow under which a document can be delivered but on the basis that it does not take effect until a condition is fulfilled (and then takes effect automatically). Escrow must be distinguished from the situation in which a document has been executed but is not yet delivered (see generally A J Bradbrook, "The Delivery of Deeds in Victoria" (1981) 55 ALJ 267).

- The present law is that the making of an unauthorised material alteration to a deed without the consent of all parties renders it void (*Aldous v Cornwell* (1868) LR 3 QB 573). It would be fairer and less arbitrary if the law in this respect were the same as that for an ordinary contract: namely, that the alteration is ineffective unless it has been agreed upon by the parties to the contract or gives rise to an estoppel.

Wider reform

59 The alternative path of reform is more radical and would involve doing away with the concept of deeds, leaving the formalities for various documents to be specified by the statute to which they relate. It is already the case that documents for registration under the Land Transfer Act must comply with the provisions of that Act. A document in registrable form is deemed to function as if it were a deed. Section 157(2) of the Land Transfer Act provides that an

instrument executed in accordance with the Act "shall have the force and effect of a deed executed by the parties signing the same". It is not a deed but has the same force and effect from the time it becomes operative.

60 If deeds were to be dispensed with, all references to them in existing legislation would have to be amended and, lest some remain undiscovered, there should be a catch-all provision to the same effect. In most instances it would seem sufficient just to provide that the document in question be signed and witnessed (in the case of an individual) or be signed in the appropriate manner for signature of formal documents by a company or other corporation (see para 65).

61 As mentioned above (at para 54) a deed must be used if a promise to confer a benefit without consideration from the person benefitting is to be made binding on the promisor. The doctrine of consideration would be overturned if the requirement for the contract to be recorded by deed were removed.

62 A section could be included in the Property Law Act along the following lines:

> A gift or promise made without consideration in circumstances where the donor or promisor intends to be bound shall be capable of being enforced by the donee or promisee if it is recorded in [an instrument executed in a formal manner].

But one then has to define the words in brackets. This, however, exposes the weakness in the wider proposal, for as long as it is thought necessary to require the use of a formal document in some circumstances, it is also necessary to define the ingredients of that document. There seems to be little point in merely changing the name of the formal document if it is to have the ingredients of a deed. In New Zealand it is relatively easy to make a deed. The limited reforms already suggested will make it slightly easier. Therefore, while the distinction between formal and informal documents is to remain, the Commission favours these more limited reforms as discussed at para 58. To go further would be to make serious (perhaps unintended) inroads into the law of contract. Furthermore, it seems to us that the requirement for the use of a deed has a protective function: a lay person will usually resort to a lawyer for its preparation and will therefore have the opportunity of taking advice on the contemplated transaction.

63 Notwithstanding our reluctance to see deeds entirely abolished we mention a possible means of avoiding the problem concerning consideration. It could perhaps be overcome by allowing a promise to be enforced if the document recording it expressly stated that the parties intended the promise to be binding even though no consideration passed from the promisee.

Covenants

64 Finally, taking a point made by Professor Burrows at 250-251, it would seem sensible to ensure that where the term "covenant" is used in the proposed new Property Law Act, it is defined so as to include contractual promises contained in writing, not just those contained in formal instruments. Indeed, implied covenants relating to leases should extend even to oral tenancies.

Questions:

Q4 Should the requirement that a deed be used be relaxed?

Q5 Should the law relating to deeds be reformed in only the limited manner set out in para 58?

Q6 Should the use of formal documentation be left to be prescribed by statute in particular situations (as with land transfer dealings) and deeds as such be abolished?

EXECUTION BY CORPORATIONS

Section 5

65 Section 5 governs the execution of deeds by corporations. It provides that a deed executed in either of two ways (under common seal or by duly appointed attorney) is deemed to have been duly executed and is binding on the corporation and, further, that all persons dealing in good faith without notice of any irregularity are entitled to presume the regular and proper execution of the deed and to act accordingly. A J Bradbrook in his article, "The Delivery of Deeds in Victoria" (1981) 55 ALJ 267, suggests that the fact that the deed is said to bind the corporation may exclude the need for delivery. We doubt that this is so but a new section should make it quite clear that a deed does not bind a corporation until delivered in the sense discussed in para 58.

Companies Bill

66 The new Companies Bill, in sections 153 and 154, provides that a company incorporated under the Companies Act may enter into a contract or other enforceable obligation. Where the obligation is of a kind which would require a deed if entered into by a natural person, section 153 will require it to be signed, depending upon the circumstances, by one or more directors or one or more attorneys. There is no requirement for the affixing of a common seal, which becomes an optional, and superfluous, extra. Section 154 then provides for the appointment of an attorney by an instrument in writing executed in accordance with section 153 and that an act of the attorney in accordance with the appointing instrument binds the company.

67 Once the Companies Bill becomes law there would seem to be no need for section 5 of the Property Law Act to extend to a company. (If it does, it must be entirely consistent with the Companies Act.) Section 5, if it were otherwise unaltered, would then be applicable only to other forms of corporation, whether incorporated in New Zealand or elsewhere, where they execute deeds governed by New Zealand law. It would also in terms of New Zealand law extend to the execution of a deed governed by foreign law where the corporation in question is incorporated in New Zealand.

68 In the case of a foreign corporation, section 5 presumes a deed to be valid if its seal has been affixed. However, quite apart from the fact that the Companies Bill signals a further move away from seals in New Zealand (see present section 4), the concept of deeds and sealing is not universal and many foreign corporations do not have, or need to have, common seals.

69 In the same way as section 153 of the Companies Bill is to govern the execution of all enforceable obligations by New Zealand companies, whether or not the document in question is in the form of a deed, it would seem to be desirable that the replacement for section 5 should have complementary coverage in relation to other New Zealand corporations, and to foreign corporations - in both cases including corporations sole. If, as seems attractive, the new section in the Property Law Act is expressed in parallel terms, it would also dispense with the need for common seals.

Public Bodies Contracts Act

70 The execution of deeds by New Zealand local authorities and other public bodies is presently governed by the Public Bodies Contracts Act 1959. That Act contains schedules listing the public bodies to which it applies, these being frequently changed by amending legislation - a cumbersome procedure.

71 Section 3 of the 1959 Act provides that where a contract, if made by private persons, must be made by deed, then, if it is made by a public body, it must be in writing under seal. (There are certain variations depending upon the nature of the body corporate and the way in which its functions are exercised.) The section goes on to provide that if the contract is of a kind which, if made by private persons, must be in writing signed by the persons to be charged therewith, it shall, if made by a public body, be made either as in the case of a deed or be signed by a member or officer on behalf of and by the authority of the public body (or by another public body which exercises the functions of the first public body). A contract which could be made orally by private persons may be made in any of the above ways or may be made orally by or on behalf of the public body by a member or officer. However, no oral contract is to be made for a sum exceeding $1,000.

72 Finally, the section provides that notwithstanding the foregoing, no contract of a public body is to be invalid by reason only that it was not made in the manner provided by the section, if it was made pursuant to a resolution of the public body or to give effect to a resolution of the public body in relation to contracts generally or in relation to that particular contract.

73 Section 4 of the 1959 Act provides for delegation to committees or officers by resolution, but subject to specified limits as to amounts.

74 There is no New Zealand legislation - other than section 5 of the Property Law Act and the Public Bodies Contracts Act - of a general nature governing execution by corporations.

English legislation

75 In England, section 74 of the Law of Property Act 1925 provides for the validity of a deed

> duly executed by a corporation aggregate if its seal be affixed thereto in the presence of and attested by its clerk, secretary or other permanent officer or his deputy, and a member of the board of directors, council or other governing body of the corporation, and where a seal purporting to be the seal of the corporation has been affixed to a deed, attested by persons purporting to be persons holding such offices as aforesaid ...

76 There is also in the United Kingdom the Corporate Bodies' Contracts Act 1960 which applies to corporations generally (other than registered companies) and provides as follows:

> (1) Contracts may be made on behalf of any body corporate, wherever incorporated, as follows:-
>
> (a) a contract which if made between private persons would be by law required to be in writing, signed by the party to be charged therewith, may be made on behalf of the body corporate in writing signed by any person acting under its authority, express or implied, and
>
> (b) a contract which if made between private persons would by law be valid although made by parole only, and not reduced into writing, may be made by parole on behalf of the body corporate by any person acting under its authority, express or implied.

77 The legislation goes on to provide in subs (2) that "a contract made according to subs (1) shall be effectual in law, and shall bind the body corporate and its successors and all other parties thereto."

Proposal

78 The provision the Commission contemplates which would replace section 5 would be consistent with the new Companies Act and would apply to any contract or other enforceable obligation entered into by a New Zealand corporation or by any corporation in New Zealand or under New Zealand law. It would provide for deeds to be executed by two or more "directors" (a term defined to cover any person occupying a position in the corporation comparable to a director of a registered company and to cover the holder of the office of a corporation sole), or one director, if there is only one. Alternatively, a deed could be signed by one or more attorneys. Other obligations could be signed or entered into orally (depending upon what the law required) by any person acting under express or implied authority of the corporation. An obligation of a foreign corporation would, additionally, be valid if it would be so regarded under the law of the place where it is incorporated had the obligation been entered into in that place and under that law.

79 Though nothing in this proposal would prevent the use of a common seal for a deed, the legal requirement would be for the requisite signatures: the seal would be legally otiose. It will be appreciated that the move away from common seals in this proposal would be in disharmony with the statutes which now govern specific forms of New Zealand corporations and provide that their obligations must where a deed is required be executed under seal: for example, section 3 of the Public Bodies Contracts Act 1959, discussed above, section 15 of the Incorporated Societies Act 1908, section 9(m) of the Industrial and Provident Societies Act 1908 (which, curiously, refers to "English law" requiring the use of a seal), section 13 of the Public Trust Office Act 1957, section 19 of the Charitable Trusts Act 1957 and section 49 of the Dairy Board Act 1961. We envisage that all of these provisions would be repealed and replaced in their operation by the new section.

80 We note in connection with the Public Bodies Contracts Act that the Law Commission has an ongoing project concerned with the status of the Crown in New Zealand law and that the Finance and Expenditure Committee of the House of Representatives on the Public Finance Act is examining the position of Crown agencies.

Questions:

Q7 Should section 5 be replaced by a new section as outlined in para 78?

Q8 Should other statutory requirements for the use of common seals (as exemplified in para 79) be repealed?

POWERS OF ATTORNEY

81 Sections 134-139 state rules governing the use of powers of attorney (including enduring powers under Part IX of the Protection of Personal and Property Rights Act 1988). They are set out in a confusing manner as a result of several amendments and additions made at different times. Our initial conclusion is that these sections can be simplified and also modified in the following respects:

- The distinction now drawn in section 135(3) and (4) between corporations aggregate and other persons acting as attorneys will be out of date when the Companies Bill is enacted and comes into force since a one person company (to be permitted thereunder) would not be a corporation aggregate. The only distinction required in the form of a certificate of non-revocation, where it is made on behalf of a corporation acting as attorney, is that the person signing it should identify the capacity in which that person makes the certificate.

- There seems to be no good reason why a volunteer who is acting in good faith and without notice of an event of revocation cannot rely upon a certificate of non-revocation as conclusive proof of the continued authority of the attorney.

- Section 135(4A) states that a certificate relating to the execution of an instrument is sufficient *if endorsed on the instrument* and signed by the attorney. The whereabouts of the certificate is not the crucial factor: the question should be whether a certificate has been given.

- Section 134A, relating to the competency of married minors to appoint attorneys, would seem to be better placed in the Minors Contracts Act.

82 The sections on powers of attorney should appear alongside those relating to deeds and execution by corporations in that part of the statute concerned with formal requirements for execution of documents.

Questions:

Q9 Should sections 134-139 be consolidated, and amended as proposed in para 81?

Q10 Are further reforms required to those sections?

III
CREATION AND DISPOSITION OF INTERESTS IN LAND

83 In this chapter we consider the formal requirements for the creation and disposition of legal and equitable interests in land, including agreements for sale and purchase, conveyances, leases and mortgages. They are now found in section 49A of the Property Law Act and in the Contracts Enforcement Act 1956. First we consider section 49A. We turn then to particular difficulties relating to leases and finally we discuss a proposal for replacing the Contracts Enforcement Act and the equitable doctrine of part performance, as has already occurred in England.

FORMALITIES FOR CREATION AND DISPOSITION

84 Since the Statute of Frauds 1677 there have been statutory requirements governing the creation or disposition of interests in land. The present statutory rules are found in section 49A of the Property Law Act, section 2 of the Contracts Enforcement Act and, in respect of leases, section 115 of the Land Transfer Act.

85 Section 49A(1) prohibits the creation or disposal of a *legal* interest in land except by a writing signed by the person creating or conveying it or by that person's agent who has been lawfully authorised in writing. The subsection also acknowledges that such an interest can be created or disposed of by will or by operation of law.

86 Section 2 of the Contracts Enforcement Act deals with the creation and disposition of equitable interests and, subject to the equitable doctrine of part performance, requires that either there be a written contract or an oral contract recorded in a memorandum signed by the party against whom the contract is sought to be enforced. (We consider below in paras 101 to 123 a proposal that this rule be tightened up so that contracts for the creation or disposition of interests in land cannot be made except by a written document setting out all the express terms.)

87 Because the creation and conveyance of legal interests in land under the Land Transfer Act, Crown land and Maori land are all governed by specific statutory requirements concerning formalities, and a form of writing is required by the Contracts Enforcement Act for any contract relating to land, the statement presently contained in section 49A(1) seems to have only one residual function: it requires the use of a formal document for a transfer of a possessory title (including one claimed against a registered proprietor in respect of which an application may be made under the Land Transfer Amendment Act 1963). Although the subsection is thus of no great practical importance, it should be retained, but in a form which expresses that function so that it is clear to the reader.

88 Section 49A(3) requires that a "disposition" of an equitable interest or trust must be in writing signed by the person disposing of it or an agent lawfully authorised in writing. It also permits such a disposition by will, which can include an oral will made in accordance with the Wills Amendment Act 1955. This subsection relates to both real and personal property. It is certainly odd that a disposition of an equitable interest in *personal* property is required to be in writing whereas that is not required for the disposition of a legal interest in the same asset. The Law Commission believes that there should be no such requirement. The subsection is inconsistent in relation to choses in action because of the stipulation that an agent must be authorised in writing: not so in section 130. Moreover, the requirement for the written appointment of an agent is also inconsistent with the Contracts Enforcement Act and should be deleted. However, subject to these changes, there seems to be good reason for retaining subsection (3): it will prevent an oral disposition of an equitable interest in land which does not require a contract (for example, a gift of land).

Questions:

Q11 Should section 49A(1) be restricted to possessory interests?

Q12 Should section 49A(3) be restricted to interests in realty and the requirement for written appointment of an agent be deleted?

FORMALITIES FOR LEASES

89 The formalities for leases are complicated by:

- section 115 of the Land Transfer Act; and
- the possibility that the doctrine of *interesse termini* survives in New Zealand. At common law a tenant had to perfect title by taking possession: until this occurred the tenant had no estate, merely a proprietary right - "an interest of a term" - coupled with a right to take possession in terms of the lease (Hinde McMorland & Sim at para 5.014).

90 This topic was the subject of a very detailed consideration from PLERC in paragraphs 12-33 and Appendix C of its *Final Report on Legislation Relating to Landlord and Tenant* (1986). Unlike the comparable provisions in the Land Transfer Act for transfers, mortgages and easements, section 115 of that Act is worded in a manner which leads to the conclusion that a lease for more than three years is "void" if it is not registered. However, it is well established by case law that such a lease, though void at law, will be enforceable in equity under the rule in *Walsh v Lonsdale* (1882) 21 ChD 9, 14-15. The court will, under this rule, treat the parties to

an informal lease for most purposes as if a legal lease had already come into existence.

91 On the other hand, a lease for less than three years can be created as a legal lease even if it is entirely oral. This is the effect of section 115(2) of the Land Transfer Act and section 49A(5)(aa). (We do not bother here with the reference in the latter subsection to deeds system land.) PLERC agreed that there should be an exception for short-term leases and that no formality should be prescribed for them. However, they recommended that the three year period be reduced to one year. We propose to follow this recommendation. (Throughout this paper references to a short-term lease therefore mean a lease for one year or less including a periodic or statutory (section 105) tenancy.) Although the members of PLERC were divided over whether an informal short-term lease should have effect as a legal lease or should be merely an equitable interest, they suggested that, if a short-term unregistered lease were to retain *legal* status, the consequences could be minimised in two ways:

- It should nevertheless be defeated by subsequent registration under the Land Transfer Act of a competing interest where that occurred without fraud; and

- An unregistered short-term lease should, where the lessee had given value and had in good faith entered into possession of the premises, have priority over (i) an unregistered interest in the land created after the lessee's entry into possession, and (ii) a prior unregistered interest of which the lessee had no actual notice at the time of entry into possession. We agree with this recommendation but think that "actual notice" should in this context be extended to include an interest notified by caveat at the time of the lessee's entry into possession, whether or not the lessee had carried out a search.

92 Since PLERC was divided, and the difference between a legal and equitable interest in this context is relatively minor, we are presently inclined to preserve the status of a short-term informal lease as a legal lease. But it should be subject to the operation of the Land Transfer Act in all respects.

93 The Law Commission provisionally proposes that the formal requirements for leases be modified in the following manner:

- Deletion from section 115(1) of the Land Transfer Act of the words "of not less than 3 years"; and

- Repeal of section 115(2) of the Land Transfer Act.

This would bring section 115 into line with sections 90 and 101; ie, it would simply prescribe the way in which

registration of a lease could be obtained in the same way as those other sections prescribe the way in which transfers and mortgages can be registered. There would be no implication that an unregistered lease is "void". Consequently it would seem to be no longer possible to argue that the assistance of *Walsh v Lonsdale* is unavailable unless the tenant has already gone into possession or done some other act of part performance - there would be nothing unenforceable about the agreement to lease.

The Law Commission proposes:

- A new section in the Property Law Act defining a short-term lease and providing that it creates a legal interest in land without need for registration under the Land Transfer Act but subject, however, to the provisions of that Act; and

- New sections to be added to the Property Law Act along the following lines:

  - abolition of *interesse termini* (for the avoidance of doubt, so that there can no longer be any suggestion that entry is required to create a legal interest in land where the term is to begin as from a future date);

  - a provision that a short-term unregistered lease would, where the lessee has given value and has in good faith entered into possession of the premises, have priority over

    - any unregistered interest in the land created after the lessee's entry into possession, and

    - any unregistered interest in the land created prior to the lessee's entry into possession, being an interest of which the lessee had no actual notice at the time of entry into possession and in respect of which no caveat was registered under the Land Transfer Act against the title to the land at that time.

94 All leases (other than short-term leases) would, of course, continue to be subject to the requirement that they be made (or recorded) in writing.

95 These reforms would extend to tenancies under the Residential Tenancies Act 1986.

Questions:

Q13 Are the proposals in para 93 thought to be a satisfactory reform?

Q14 Should a short-term lease have legal status?

"NO REGISTRATION" CLAUSES

96 A further problem which has been identified in relation to leases concerns the increasingly common stipulation in commercial leases that the lessee is not to be entitled to a registered lease. Under the rule in *Walsh* v *Lonsdale* (see para 90), the holder of an equitable leasehold interest (in New Zealand terms, an unregistered lease) is treated for most purposes as if a legal lease had already been executed. However, the basis of the doctrine is that the court recognises the equitable lease as a contract for the grant of a legal lease, the lessee being entitled to an order for specific performance of that contract. It then deals with the position as if a legal lease had actually come into existence pursuant to such an order. But in New Zealand, with the exception of the short-term lease just discussed, a legal lease means one which has been registered under the Land Transfer Act. If the agreement for the lease specifically precludes registration, it necessarily precludes the granting of a legal lease. Therefore, though no doubt in an unintended way, a "no registration" clause may undermine the rule in *Walsh* v *Lonsdale* by preventing the court from granting specific performance. If so, there is arguably no interest in the land vested in the tenant, whose remedy would be confined to damages for breach of the lease agreement if the lessor repudiates it.

97 Case law already establishes in other contexts that a tenant who has lost the right to specific performance is unable to rely on the rule in *Walsh* v *Lonsdale*. For example, where the tenant is in such serious breach of covenant that the court would deny specific performance, or where the grant of a formal sublease would be in breach of the covenants of the head lease, or where an agreement for lease is dependent on a condition which has not been met, a court of equity will not give assistance under the rule in *Walsh* v *Lonsdale* (see *Coatsworth* v *Johnson* (1886) 54 LT 520; *Clemow* v *Cock* [1920] GLR 70; *Upper Hutt Arcade Ltd* v *Burrell* [1973] 2 NZLR 699 and *Australian Mutual Provident Society* v *400 St Kilda Road Pty Ltd* [1990] VR 646).

98 It may be that a court would have little hesitation in recognising that in New Zealand the rule in *Walsh* v *Lonsdale* requires some modification in relation to the Land Transfer system. However, it would seem to be a wise precaution to spell out the court's power to grant specific performance - upon which the existence of any equitable interest in land is dependent - regardless of a "no registration" clause. That would enable the court to enforce the lease as an interest in land without requiring the lessor to execute a lease in

registrable form or requiring registration. The bargain between the parties would be preserved but the lessee would have an interest in land protectable by caveat.

99 A provision along the following lines is tentatively suggested:

> (1) A form of writing expressed as a grant or agreement for the grant of an interest in land may in the court's discretion be specifically enforced and may operate as an interest in that land notwithstanding any agreement that the grant shall not be registered under the Land Transfer Act 1952.
>
> (2) In this section "grant" includes a lease, mortgage or easement.

100 Subsection (2) recognises the fact that a similar problem could exist if a mortgage or easement document contained a "no registration" clause. It could also be stipulated that the court should not override the contract by requiring registration.

Question:

Q15 Should the court be able to enforce a lease as an interest in land despite a "no registration" clause?

REQUIREMENT FOR A WRITTEN CONTRACT

101 If it is accepted that there is good reason for requiring land contracts to be in writing or evidenced in writing, then the new Property Law Act could either incorporate a version of section 2 of the Contracts Enforcement Act or could follow the Law Commission in England in its Report No 164: *Transfer of Land: Formalities for Contracts for Sale etc of Land* (1987), the recommendations of which were promptly passed into legislation in section 2 of the Law of Property (Miscellaneous Provisions) Act 1989.

Criticisms of present law

102 The Law Commission in England was very critical of the existing law, ie, the combination of what is in New Zealand section 2 of the Contracts Enforcement Act 1956 and the equitable doctrine of part performance. It summarised the existing position as follows:

> Contracts which do not comply with the requirements of the section are not void, but are merely unenforceable by action. They are valid and can have effect provided they are enforceable in some other way than by action. Thus, if a purchaser pays a cash deposit to the vendor under an oral contract, the vendor may keep that

> deposit if the purchaser defaults. The section does not avoid oral contracts, but only bars most of the legal remedies by which they may be enforced, and it does so as a matter not of substance but of procedure which, like periods of limitation, must be specially pleaded in order to be relied on. Furthermore, it actually allows oral contracts, provided they happen to be evidenced in writing, for all that is required is that a written memorandum of the contract should have come into existence. (para 1.3)

103 The Commission commented in relation to the equitable doctrine of part performance:

> As a result of judicial attempts to prevent the statute being used as an instrument of fraud, it is virtually impossible to discover with acceptable certainty, prior to proceedings, whether a contract will be found to be enforceable under the statutory requirements.
>
> The decision in *Steadman* v *Steadman* [1976] AC 536 has left the doctrine of part performance in a most uncertain state. Although it was decided that mere payment of a sum of money in the circumstances of the case amounted to a sufficient act of part performance, it was left open as to whether the acts performed need indicate a contract relating to land. In addition, the majority of the Law Lords severally indicated that, in the ordinary circumstances of a contract for the sale of land, a sufficient act of part performance could be found in the fact of the purchaser instructing solicitors to prepare and submit a draft conveyance or transfer. In consequence, it appears that an oral contract for sale can readily and unilaterally be rendered enforceable and the provisions of [the section] left to beat the air. (paras 1.8 and 1.9)

104 That Commission was also critical of what it saw as the one-sided effect of the present law, namely that a party who is not bound, because his or her signature nowhere appears, can elect whether or not to enforce the contract against the other party who has signed it or a memorandum. The position is, in fact, not quite as one-sided as the English report makes it appear - though the criticism is still valid - since the means by which the non-signing party elects to enforce the contract, namely the commencement of legal proceedings, will necessarily create a memorandum of the contract which is binding on the non-signing party.

105 We also note the interpretation of *Steadman* v *Steadman* by Mahon J in *Boutique Balmoral Ltd* v *Retail Holdings Ltd* [1976] 2 NZLR 222. He held that it was insufficient merely to show that the acts of alleged part performance were performed in reliance on a contract with the defendant which was consistent with the contract alleged. In the opinion of Mahon J the plaintiff must show that the act relied upon was in part performance of the contract and that the act was done in compliance with a contractual obligation.

106 Nevertheless the present amalgam of ancient statute law - originally dating from 1677 - and the attempts of equity to avoid misuse of the statute have certainly resulted in a situation which is sufficiently lacking in logic that it is difficult to explain to lay people. It is full of anomalies and great difficulty is often found in determining not only whether an oral contract has been made but also whether it has become binding either by reason of a memorandum or part performance. It is therefore easy to agree that the law on this subject is ready for reform, if a sensible alternative can be found.

Should writing be required?

107 The Law Commission in England considered and rejected simple repeal of the section and concluded, in an English conveyancing context, that this could not be recommended. It was noted that there was "absolutely no support for this proposal" (para 2.6). "Some thought it quite irresponsible." (But see M G Bridge "The Statute of Frauds and Sale of Land Contracts" (1986) 64 *Canadian Bar Review* 58 for a contrary view.) The principal justification for continuing to require formalities for contracts dealing with land was thought to be the need for certainty.

> The existence and terms of oral contracts are always difficult to establish and the resulting confusion ... would, we anticipate, lead to increased litigation. To minimise disputes, reliable incontrovertible evidence of the existence and terms of a transaction needs to be available for later reference. In light of this, the value of the evidential function of writing cannot be doubted. (para 2.7)

108 That Commission also thought that reform should not increase the likelihood of contracts for the sale or other disposition of land becoming binding before the parties had been able to obtain legal advice. As a consumer protection argument the Commission noted that, for most people, contracts for the sale of land are important transactions involving them in major financial commitments and general upheaval. "In such circumstances, it appears vital that a consumer takes all reasonable precautions and is fully protected" (para 2.9).

109 Even allowing for the differences between conveyancing procedures in England and New Zealand, these arguments have considerable force in this country. We recognise, like the English Commission, that contracts for various forms of personalty, particularly shares, may have the same financial significance. It may therefore appear slightly odd that many such contracts can be made without any formalities at all, a situation which does not appear to have given rise to particular difficulties of proof. However, such of those transactions as are done orally usually involve very straightforward dealings. Few, if any, land transactions are straightforward in the same way as a sale and purchase of shares listed on the Stock Exchange, though they may appear so to the outside observer. (Outside the Stock Exchanges, share

sales would normally be the subject of a written agreement and on the Exchange the brokers on each side take immediate steps to record each transaction.) But there is always the need to carry out a title search for the purpose of determining whether the vendor is the registered proprietor, whether there are encumbrances and for checking the dimensions. Town planning and other matters within the purview of the local authority should be investigated. Contracts in relation to land which have the appearance of the greatest simplicity - for example, the sale and purchase of a section of bare land - can very easily go awry. The parties need the protection of a written record of their bargain. If they are required to contract in a manner governed by certain formalities, there is a much better chance that they will use a form of agreement which has been found to be generally acceptable, such as the form approved by the New Zealand Law Society and the Real Estate Institute and in general use throughout New Zealand. No such necessity arises in relation to the sale of shares on a Stock Exchange or for many other transactions involving forms of personalty.

110 While, therefore, it would be inappropriate to prescribe formalities for personalty generally and people should be left free to choose the form of written contract (if any) which is appropriate to their dealings with personalty except where consumer protection legislation directs otherwise (eg, Door to Door Sales Act 1967 and Hire Purchase Act 1971), we believe that it remains good policy to require of persons dealing with interests in land that the express terms of their bargain be recorded in writing. Since the anomalies in the present law have largely arisen from the fact that a land contract does not need to be made in writing, but merely recorded in writing, it is logical to conclude, as did the Law Commission in England, that a more workable rule might involve a mandatory requirement that contracts relating to interests in land *must* be actually made in writing; that is, oral contracts for interests in land should be prohibited and consequently could not exist so as to be capable of "part performance".

111 The Law Commission in England considered and rejected some alternatives: slight amendments to the section, particularly attempting to define the doctrine of part performance; the use of prescribed forms; cooling off periods. They quickly found that none of these was really workable. We think that prescribed forms would be inappropriate unless some way could be found to design a set of forms which covered every type of transaction and every conceivable situation. We note that the use of a cooling off period for certain kinds of conveyancing transactions has been legislated in some Australian states. At this stage of our researches the Law Commission would not feel confident about recommending such a course for New Zealand, if only because it must surely lead to further complications and delays in an area already criticised for exactly these faults. But we are continuing to examine the possibility and would welcome the views of those who have had practical experience of cooling off periods.

The English reform

112 The conclusion reached in England was that the law should require land contracts to contain all the express terms - leaving room for other terms to be implied as a matter of fact or law. The effect of this would be that no contract in relation to land could come into existence unless it complied with the statute. There would be no room for oral contracts (or memoranda of them) or the doctrine of part performance, there being no contract to be performed unless the statutory requirements were met. In England the express terms must now be stated in one document, signed by all the parties (on one or more copies). They can either be set out in that document or can be incorporated by reference made in that document.

113 Quite apart from the difficulty that may be caused by any such reform to people who mistakenly fail to comply and are accordingly left without the "contract" on which they may have relied, we think that this formulation is too rigid. It would appear to preclude any binding effect where an offer signed by the offeror contains all the express terms but is accepted, not by endorsement of the offeree's signature on a copy of the offer document, but by a separate document signed by the offeree which refers to and accepts the offer. We see no good reason for this distinction. The latter method is a logical and appropriate means of recording a bargain.

114 Some thought would also need to be given to options, including rights of renewal in leases. In New Zealand an option document is usually signed only by the grantor. In a case on the English statute it has been held that an option must be signed by both parties but that an exercise of option need only be signed by the purchaser (*Spiro* v *Glencrown Properties Ltd* [1991] 1 All ER 600). Perhaps the same difficulty will not arise in relation to renewals of lease since the renewal clause is contained in the lease document itself and that is signed by both parties. Nevertheless it seems better to allow an option contract to exist where it is signed by the grantor only. The signature of the holder will appear in the document which exercises it.

115 In New Zealand the parties may simply execute a document in registrable form without bothering to have a prior written agreement. This frequently occurs when a mortgage, easement or profit is being created. If the English reform were to be followed here - about which we have not reached any conclusion - it would therefore be necessary to ensure that such a document was legally effective even though it might not be signed by both parties, provided it was adequately executed for the purposes of registration under the Land Transfer Act.

Remedies if contract not in writing

116 We come at this point to the matter which causes us the most hesitation in following the path so recently trodden in England. What happens to the "parties" who have purported to enter into a land contract and find that because of the statute they have no contract? The equitable doctrine of part

performance developed because some parties to oral contracts sought to withdraw from them in circumstances which were felt to merit the intervention of equity to protect those who had relied upon the bargain. The Law Commission in England considered whether the abolition of part performance would remove this protection in some cases where it really should be available. It found several means whereby a court of equity could render assistance. First, it was said that the ability of a court to *rectify* a contract where a term had been omitted or wrongly recorded would continue. It also considered that the courts could often find that terms which were not recorded in terms of the new statute in fact formed a *collateral contract*. This belief seems to be justified. In *Record* v *Bell*, a case in the Chancery Division, reported in *The Times* on 21 December 1990, it was held that where a contract in two parts for the sale of land, signed by the respective parties, was awaiting exchange and the vendor then offered a warranty as to the state of the title in order to induce the purchaser to exchange, the acceptance of that offer by the purchaser could amount to a collateral contract outside the requirements of the 1989 Act so that, the contracts having been exchanged, the parties were bound.

117 *Restitutionary relief* would also be available such as, for example, requiring a "vendor" under an oral "contract" to restore to the "purchaser" a deposit paid by the latter.

118 But perhaps the most useful form of equitable relief which might (and, we think, would) remain available would be the use of *equitable estoppel* where one party has acted in a manner which represents to the other that there is a contract and that it will be performed, and the other, to his or her detriment, relies upon that representation.

119 Estoppel is a very flexible remedy, particularly now that the courts have begun to move away from rigid technical requirements, as by treating the probanda in *Willmott* v *Barber* (1880) 15 ChD 96 as guidelines rather than mandatory requirements. It may even be that in some circumstances parties who could not rely on the equitable doctrine of part performance, because of the requirements which remain even after *Steadman* v *Steadman* (para 103), could in some circumstances succeed in obtaining relief based on estoppel. It is interesting to consider how a case such as *Boutique Balmoral Ltd* v *Retail Holdings Ltd*, where the plaintiff failed in a claim based on enforcement of the agreement to lease, might have concluded if at the present day it were argued on estoppel and with a glance at *Walton's Stores (Interstate) Ltd* v *Maher* (1988) 62 ALJR 110. The law is certainly moving in the direction of allowing equity to intervene wherever a defendant has acted unconscionably. As was said in *Ashburn Anstalt* v *Arnold* [1989] Ch 1, 22, by the English Court of Appeal in the context of a claim based on constructive trust:

> The test ... is whether the owner of the property has so conducted himself that it would be inequitable to allow him to deny the claimant an interest in the property.

Thus, the new statutory formal requirement might combine both the certainty of a written contract containing all the terms with the availability of a truly flexible equitable remedy capable of dealing with abuses in a manner which is more satisfactory than the relatively rigid equitable doctrine of part performance.

120 However, it is important to recognise that the equitable jurisdiction based on the use of estoppel or resulting or constructive trusts does not necessarily lead to enforcement of the oral bargain as is the case where the plaintiff is successful in claiming on the basis of part performance. In some circumstances enforcement of an oral "contract" may be the appropriate form of relief. But in many others, perhaps the majority of cases, the court may well conclude that it is best that the parties simply be restored to their former positions with the plaintiff being compensated for any loss caused by reliance upon the assurances given by the defendant. The object of equity is to avoid detriment, not to fulfil the bargain (Brennan J in *Walton's Stores (Interstate) Ltd* v *Maher* (1988) 62 ALJR 110, 125). And see generally *Baumgartner* v *Baumgartner* (1988) 62 ALJR 29 and *Gillies* v *Keogh* [1989] 2 NZLR 327 (CA) dealing with claims between unmarried but cohabiting parties, a context in which bargains relating to land are frequently made informally. We observe that the courts seem to be able to cope with such situations and have developed considerable flexibility of remedy. The position in England for such persons subsequent to the 1989 legislation is considered by Professor David Hayton in "Equitable Rights of Cohabitees" (1990) Conv 370.

121 The assistance which a court of equity can give is, however, dependent upon proof of the relevant facts, particularly reliance. An immediate difficulty is that it might not be available if the plaintiff could be shown to have been well aware of the new statutory rule. Take, for example, the case of two people on friendly and trusting terms, who, in full knowledge of the statute, elect to make a long-term arrangement for a lease orally or in an informal document which does not comply with the statute. The "lessee" enters and fits out the premises at significant expense. The "lessor" then repudiates and seeks possession. Would the court deny the "lessee" protection because he or she knew that the arrangement was not a contract for a lease? Or would it say that the lessee relied upon the assurances which amounted to a promise by the "lessor" not to invoke the statute and that a promise of no force at law can nevertheless be enforced in equity? We incline to the view that the latter would be the answer (*Walton's Stores (Interstate) Ltd* v *Maher*). But:

- would all the hard cases be able to be accommodated? and

- is it too much of a leap of faith to follow the English lead before the principles now being formulated in the equity jurisdiction have become rather more certain? Would this, in other words,

> be replacing one complex and uncertain rule with another which, if not complex, would in the meantime have uncertain elements?

Even if the answers to these questions are in favour of the reform, we think that the equitable remedies ought to be mentioned in the new section as an indication to the courts. The section should state that it does not affect

- resulting, implied or constructive trusts
- restitutionary relief (which would include an action for money had and received)
- any estoppel, or
- any collateral contract.

This has not been done in the English Act apart from a reference to resulting, implied or constructive trusts.

Exceptions

122 The Law Commission in England also pointed to the need for certain exceptions to the new statute. One of these was the short-term lease (which is consistent with the conclusions which we have reached on this topic in para 91). Another is where the transaction takes place by way of public auction. The present law is that the auctioneer is impliedly authorised to act as the agent of both the vendor and the purchaser to sign the form of contract after the auction (***Emmerson*** v ***Heelis*** (1809) 2 Taunt 38; 127 ER 989). The English Law Commission commented:

> If sales by auction were to be included in our new provisions, there would be no contract at all until the auctioneer had signed, so that it might be open to either party to withdraw. Special provisions could have been devised to ensure that this would not happen, but these would have to be quite complex to ensure that auctions would not become legally hazardous. On further reflection we have decided that it is not necessary to insist on writing to validate a contract made at auction. The present situation where a contract is made at the fall of the hammer has caused no difficulties. We appreciate that the effect of our recommendation is that it will no longer be necessary for any written memorandum to come into being. However, at present the memorandum can come into existence and may be signed without actually involving the parties themselves. It is thus not a formality which necessarily serves the function of warning people what they are doing or making sure they understand the importance of the contract. There is little doubt that in the vast majority of cases the terms of the contract will continue to be put into writing, and if they were not, the courts would readily decide any dispute as to terms as they now do with other oral contracts.

> However, we propose confining this exception to public auctions since other forms of auction would still seem to call for the protective functions of formalities. (para 4.11)

123 It was also pointed out that a contract to sell a company debenture, where it charges the land of the company, is a species of contract for an interest in land. To the extent that these are traded by oral contract on a Stock Exchange, there would seem to be the need for an exemption for those trades.

Contracts of guarantee

124 We mention at this point contracts of guarantee since they also fall within section 2 of the Contracts Enforcement Act. Experience suggests that difficulties of the kind found in relation to land transactions have not arisen in relation to guarantees because in practice they are entered into as if the legal rule were that a contract of guarantee must be in writing. They are rarely documented by way of memorandum of an oral guarantee previously given. Moreover, it seems that the doctrine of part performance has no application to a contract of guarantee (*Maddison v Alderson* (1883) 8 App Cas 467, 490). It would be difficult to satisfy the requirements of the doctrine by showing that acts done by the creditor were referable to the guarantee (O'Donovan and Phillips at 92).

125 We believe that no dislocation to present practice would be caused by a direct requirement that, to be binding, a contract of guarantee must be actually entered into in writing signed by the guarantor. There seems to be no good reason for requiring signature by the beneficiary of the guarantee. Alternatively, the present law, namely that either a written contract or a signed memorandum of an oral contract of guarantee must be found, could be preserved but it could be expressly stated that the doctrine of part performance does not apply. We presently favour the first course, which, as we have said, seems aligned with present practice. In either case the provision which appears in section 3 of the Contracts Enforcement Act making it unnecessary to state in writing the consideration for the guarantor's promise should be preserved. That dispensation has not, so far as we are aware, given rise to any problems.

Questions:

Q16 Should a form of writing be required for the creation and disposition of interests in land?

Q17 Does the present law (Contracts Enforcement Act modified by the equitable doctrine of part performance) operate in an unsatisfactory manner?

Q18 Should a cooling off period be introduced?

Q19 Should all express terms be required to be recorded as set out in paras 112 to 115 (modified version of 1989 English statute)?

Q20 If so, would available equitable remedies be adequate to temper the effect of the statute as part performance now does?

Q21 Would there be a need for exceptions other than those referred to in paras 122 and 123?

Q22 Should the formal requirements for guarantees be modified as suggested in para 125?

IV
REFORM OF GENERAL PROPERTY RULES

REPLACEMENT OF QUIA EMPTORES

126 The statute known as Quia Emptores (1289-90) 18 Edw 1, St 1, cc 1 and 3 is usually regarded as having abolished subinfeudation. This occurred when A as tenant in fee simple granted land in fee simple to B (so that B held it from A subject to the incidents in the grant to B). The source of the abolition is not free from doubt. (It may actually derive from 1 Edw 3 St 2, which is mentioned below.) The history of the matter is traced in *Re Holliday* [1922] 2 Ch 698 which contains examples of subinfeudation and confirms that it is certainly a prohibited practice.

127 Free tenants who did *not* hold directly from the Crown (ie, who held from a subject) were granted by Quia Emptores the right to alienate land by substitution without first having to obtain the lord's consent and without payment of a fine. The orthodox view has been that in empowering the free alienation of land, Quia Emptores is the first stone in the foundation of the land law of common law jurisdictions. Closer analysis has nevertheless revealed that the Act would never have applied at all in New Zealand without later legislation. The doctrine of tenure applies in New Zealand but all landowners here hold their land directly from the Crown. As to the doctrine of tenure in New Zealand see *Veale* v *Brown* (1868) 1 NZCA 152 at 156-157.

128 The removal of the limits on the freedom of tenants holding their land directly from the Crown to alienate it began in 1327 with the enactment of 1 Edw 3, St 2, cc 12 and 13. Tenants in chief remained liable to pay a fine or levy to the King when they exercised this right. In 1660, section 4 of the Tenures Abolition Act (12 Car 2, section 24) turned all such tenure into free and common socage (freehold tenure) and brought it under the operation of Quia Emptores on the same footing as if the King were a subject (*Re Holliday* at 713). From then on fee simple estates were freely transferable in the same way as lesser interests.

129 Section 35(2) of the Guardianship Act 1968 repealed the Tenures Abolition Act 1660 in New Zealand. There has been some debate about the effect of the repeal. It seems to have been thought at the time that this did not effect a change in the law because the 1327 Act continued in force. However, PLERC in its *Report on the Imperial Laws Application Bill* (1985) considered that section 4 of the Tenures Abolition Act 1660 should be reinstated.

130 Nevertheless, when the Imperial Laws Application Act 1988 came into force on 1 January 1989 Quia Emptores was preserved but the 1327 Act was not; nor was the Tenures Abolition Act 1660 reinstated.

131 As a result it is arguable, at least in theory, that there is no current legislative authority in New Zealand for the alienation of land granted by the Crown after 1 January 1989, though it can be imagined that a judge would strenuously strive to avoid this conclusion. It would seem prudent to put the matter beyond doubt and to declare that grants from the Crown in fee simple, whether before or after the Act, are to be taken to be in freehold tenure (the modern name for free and common socage) and that subject to the terms of any statute (such as the Reserves Act 1977) or any Crown grant or lease, estates or interests in land are and have always been freely transferable. Interests in land would be transferable "freely", namely without the Crown or a reversioner being able to ask for payment of any money unless that had been specifically provided for in a statute or in the instrument under which a leasehold interest in land arose.

132 It would also seem to be desirable to confirm that subinfeudation in fee simple continues to be prohibited - just in case someone (possibly for tax reasons) attempts to engage in this practice. PLERC concluded that the appearance of subinfeudation in New Zealand, as even a theoretical possibility, might create unnecessary complication.

GENERAL RULES IN PART II

133 Part II of the Property Law Act consists of a miscellany of largely unrelated rules, many of which are of ancient origin. Sections 14 to 32, 34 and 40 date from before 1908. Most of them were in the Conveyancing Ordinance 1842. Sections 35 to 38 were added to the Act in 1952. Sections 33A and 33B (which deal with human rights issues) came in 1965 and 1977 respectively. Section 40A concerning property agreements between persons cohabiting as husband and wife was inserted in 1986.

134 Some of the sections were intended to abolish rules of common law. Section 26 does this entirely in relation to the prohibition of a possibility upon a possibility. Its work of abolition having been done, it need not now be repeated. Certain other sections are not couched as direct abolitions despite their section headings (sections 15 and 17) or, having abolished a rule of the common law, go on to make provision for what should happen if anyone thereafter tries to rely upon the abolished rule (sections 16 and 22 dealing respectively with estates tail and the rule in *Shelley's* case). The Commission thinks that these sections can best be dealt with by restating the abolition in direct language followed (in the case of sections 16 and 22) by a restatement of the consequential provisions.

135 Sections 18 (freehold in future may be created), 19 (estate in chattel real may be created by deed), and 21 (rights of entry, etc) contain modifications of fundamental common law rules affecting property. They cannot be understood by themselves without looking to the principles which they alter. The Commission favours direct statements of those rules in their modified form so that some of the

obscurity of the present sections can be removed, but it is not intended to make further changes to the rules themselves.

136 Section 14 which declares that certain limitations may be made by direct conveyance without the intervention of uses dates from before the repeal in New Zealand of the Statute of Uses. It is no longer necessary.

137 We have already, in dealing with the repeal of Quia Emptores (para 131), recommended confirmation of the rule that all estates or interests are freely transferable. To this we suggest that there be added sections declaring that:

- future interests in property may be freely created within the limits permitted by the rule against perpetuities (as modified by the Perpetuities Act 1964);

- every estate or interest in property (including future, executory and contingent estates or interests) may be freely created or conveyed by deed or will; and

- a life estate may be created in relation to a lease (which was not possible at common law).

138 Sections 29 (equitable waste), 32 (corporations may hold as joint tenants), 34 (disclaimer of powers), 35 (intermediate income of contingent or executory gifts), 36 (receipts for income by married infants), 37 ("heirs" and other words interpreted), 38 ("heirs of the body" and other words interpreted) and 40 (appointments valid notwithstanding objects excluded) should, the Commission believes, be repeated in the new statute though we would hope that this could be done in plainer language. The rules which they lay down or confirm do not seem to require any amendment in substance and should be preserved.

Contingent remainders

139 A contingent remainder is a remainder in land expressed to take effect upon the occurrence or fulfilment of an event or condition which may never occur or be fulfilled or which may not occur or be fulfilled until after the determination of the preceding estate in the land. We think that it would be helpful if a section to take the place of section 20 contained a definition along these lines.

140 Subsection (1) of section 20 reverses two separate common law rules. The first was that a contingent remainder was void unless it was limited in such a way that it could vest during the continuance of the estate preceding it or at the moment that estate determined, and unless it did in fact so vest (Hinde McMorland & Sim at para 4.020). For example, the remainder was void where there was a limitation:

> to A for life, remainder to such child or children of his as shall attain the age of 21 after his death.

In terms of the disposition itself, the remainder could not vest either during or immediately on the termination of the preceding estate, and so would be struck down. Further, a contingent remainder would be struck down by the common law if the preceding estate in fact came to end before the remainder vested. For example, in the case of a limitation:

> to A for life, remainder to B when he attains 21

B's remainder would be destroyed if A died before B reached 21.

141 The first part of subsection (1) saves a limitation of this kind. It is suggested that this be restated in the following, or similar, manner:

> A contingent remainder shall not be void by reason only of the fact that it cannot take effect when the estate immediately preceding it for any reason ceases.

142 The second part of subsection (1) reversed the common law rule that the preceding estate which supported a legal contingent remainder had to be an estate of freehold (such as a life estate), because an estate of leasehold did not carry seisin (Hinde McMorland & Sim at para 4.019). A revised version of this part of the subsection could be as follows:

> A contingent remainder may be created so as to take effect upon the termination or expiry of a leasehold estate.

143 Subsection (2) of section 20 reversed the rule that if a life estate and a fee simple remainder or reversion became vested in the same person in the same right, any intermediate contingent remainder was destroyed (Megarry & Wade at 193-194). This could be restated:

> Two estates vested in the same person shall not merge where they are separated by a contingent remainder or interest.

Restriction on executory limitations

144 Section 23 is intended to ensure that a provision for a gift over on default or failure of issue of a person holding an estate or interest in property cannot operate once one of the relevant issue has reached the status of an adult. Prior to the Wills Act 1837 a limitation in respect of land

> to A, but if he shall die without issue, to B

would confer on A an estate tail with remainder to B. The reason was that B's interest could be defeated by conversion by A's interest into a fee simple (Hinde McMorland & Sim at para 4.023). Section 29 of the Wills Act 1837 changed this position. The section produced the result that A took an estate in fee simple in the land subject to a gift over to B, if at A's death there was no issue of A then living. But this

left the position very uncertain. "A could seldom be sure whether or not a gift over to B would take effect. However many children or grandchildren A might have, they might all predecease him so that he would 'die without issue'" (Hinde McMorland & Sim at para 4.023). Section 23 of the Property Law Act removes this uncertainty. The executory limitation over to B now becomes inoperative as soon as any issue of A attains the age of 20. As Hinde McMorland & Sim put it:

> Therefore, if section 23 applies, A's interest becomes absolute either:
>
> (1) If any issue of A attains the age of 20 (even if none survives A); or
>
> (2) If A dies leaving any issue (even if not attaining the age of 20). (para 4.023)

145 Section 23 should, the Commission thinks, be re-enacted in a more approachable modern form and should, like its English equivalent (section 134 of the Law of Property Act 1925) and its New South Wales equivalent (section 29B of the Conveyancing Act 1919) relate to all types of property, not just, as at present, to land. We suggest the following formulation for consideration:

> (1) When the estate or interest in property held by any person is expressed to be subject to a gift over on default or failure of all or any one or more of the issue of that person (whether within or at any specified period of time or not), the gift over shall be void and ineffectual as soon as the relevant issue or any of the class of relevant issue at any time attains 20 years of age.
>
> (2) In this section a "gift over" includes a gift upon the determination by any means of any estate or interest.

146 The existing section applies only where the gift over is contained in an instrument coming into operation on or after 1 January 1906 (the date of commencement of the Property Law Act 1905 where the reform was first made). The Commission thinks that it is now probably unnecessary to preserve this exemption, all pre-1906 gifts over having, in all reasonable probability, either operated or failed.

Merger

147 Section 30, which says there shall not be any merger by operation of law only of any estate the beneficial interest in which would not be deemed to be merged or extinguished in equity, may now be superfluous. It is intended to make it clear that the equitable rule on merger must prevail over the common law rule (*In re Waugh, Sutherland* v *Waugh* [1955] NZLR 1129). But this is sufficiently achieved in general terms by

section 99 of the Judicature Act 1908. It therefore does not seem necessary to repeat section 30.

Rentcharges

148 A rentcharge is, as its name indicates, a charge on land for the purpose of securing a rent. "Rent" is defined in section 2 of the Property Law Act as including yearly or other rent and also any "toll, duty, royalty or other reservation by the acre, the ton, or otherwise". A charge is included in the definition of "mortgage" in section 2 of the Act. A rentcharge is also included in the definition of "mortgage" in section 2 of the Land Transfer Act. That Act prescribes a form of memorandum of encumbrance to secure a rentcharge over Land Transfer land.

149 Elsewhere we affirm the recommendation of PLERC that the lessor's right under a lease to distrain be abolished (para 569). We think that the right to distrain should also be abolished in relation to a rentcharge. This can be done by the repeal of section 5 of the Landlord and Tenant Act 1730. There will then be an even closer similarity of a rentcharge to a mortgage under New Zealand law.

150 Nevertheless, a rentcharge is distinct from a mortgage. Despite section 81 of the Property Law Act it cannot be redeemed in the same way as a mortgage (see, however, section 151). In the case of a mortgage the debt is the principal thing and the security is merely the accessory. At least in theory the principal thing in the case of a rentcharge is that the money is to be paid out of the land. Consequently enforcement action is against the owner for the time being of the land rather than against the original grantor. But in practical terms, whether the charge is a mortgage or a rentcharge, in the event of default the chargeholder is likely to look first to the owner of the land for payment before exercising the security against the land.

151 Rentcharges have been a valuable mechanism to bind successors in title to perform positive covenants. At common law the burden of a covenant did not run with the servient land. In equity only the burden of negative covenants could run with the land (Hinde McMorland & Sim at para 11.028). The advantage which a rentcharge had over a mortgage was that "a rentcharge, unlike a mortgage at common law, is not required by its nature to be redeemable" (Goodall and Brookfield at 321).

152 But now section 64A of the Act (inserted by the Property Law Amendment Act 1986) allows for successors in title to be bound in equity by positive as well as restrictive covenants relating to other land and section 126A authorises the noting of them against the Land Transfer Register. So this function of rentcharges has become unnecessary. But they continue to be used as a means of securing covenants in gross, particularly by local authorities, though we understand that the need for this device may diminish after enactment of the Resource Management legislation now before Parliament.

153 Section 31 dates from 1842 and is (apart from section 150 which relates to deeds system land only) the sole direct reference in the 1952 Act to rentcharges. It provides that the release from a rent of any part of the land out of which it is payable shall not be a discharge of the residue of the land from the rent. It reverses the common law rule. It also contains a proviso that where the owner of the part released is not the owner of the residue charged with the rent, the owner of the residue is to be entitled to the same contribution from the owner of the part released as he would have been entitled to if no release had been made.

154 Apparently the reason for the common law rule was the original view that a rentcharge was one entire right issuing out of every part of the land charged (Garrow at 443). As the Property Law Act is overridden by the Land Transfer Act, the first portion of section 31 may be redundant for practical purposes. Section 111(1) of the Land Transfer Act provides for the registration of a discharge of the whole or part of the land comprised in any mortgage (including a rentcharge). Upon registration of a partial discharge of mortgage, the portion of land discharged is released from liability (section 111(2)) but the charge will remain registered against the residue. However, if section 31 were to be repealed, there might be doubt about the position under unregistered rentcharges. Likewise, repeal might create doubt in connection with the right of the owner of the residue of the land to claim contribution, as is now provided for in the proviso to section 31. The Commission therefore believes that the substance of section 31 should be brought forward into the new Act.

Human rights provisions

155 Sections 33A and 33B, together with section 110(1A), are misplaced in the Property Law Act since, although they relate to property, they are plainly provisions of a human rights nature. Section 33A makes void any provision which has the effect of prohibiting or restricting a disposition of property (orally or in writing) to any person by reason only of the colour, race or ethnic or national origins of that person or a family member. If a licence or consent to an assignment of subletting, charge or parting with possession of leased premises is withheld on any of those grounds, it is by section 110(1A) declared to be unreasonably withheld.

156 Section 6 of the Race Relations Act 1971 was passed after section 33A was enacted. Broadly, it provides that it is unlawful for anyone to discriminate in connection with *real* property by reason of the colour, race or ethnic or national origins of any person. It covers a wider range of activities than section 33A - including a *refusal* to make a disposition of real property, which clearly does not fall within section 33A. On the other hand, section 33A applies to dispositions of personal property as well as real property.

Section 4 of the Race Relations Act dealing with the provision of goods and services to the public may also be relevant in some circumstances to a situation covered by section 33A. But it seems that nothing in the Race Relations Act would, for example, strike down a provision in a lease of a chattel that it shall not be permitted to be used by anyone of particular racial origin. Section 33A therefore appears to be performing a valuable function. Section 25 of the Human Rights Commission Act 1977 parallels section 6 of the Race Relations Act in relation to discrimination etc by reason of the sex, marital status or religious or ethical belief of any person. It again relates only to land. Section 24 of that Act parallels section 4 of the Race Relations Act.

157 The discrepancies in the various Acts may have arisen from the piecemeal way in which they were enacted. A provision along the lines of section 33A certainly should be retained but someone consulting the Race Relations Act or the Human Rights Commission Act may completely overlook the existence of a relevant section hidden away in the Property Law Act which is not where users of those other Acts might expect to find such subject matter. The Law Commission therefore considers that it would be appropriate if amendments were made to the Race Relations Act to bring within it the prohibitions now found in section 33A and section 110(1A). A parallel provision dealing with discrimination by reason of sex, marital status or religious or ethical beliefs could be put into the Human Rights Commission Act.

158 Section 33B makes void a provision in connection with the disposition of property (orally or in writing) to the extent that its effect is to require any party to the disposition or a successor in title or the spouse of any such person to be or to undertake to become sterile. It is perhaps surprising that this is not found in the Human Rights Commission Act (especially since both section 33B and that Act were passed in the same year - 1977). The Commission suggests that section 33B should be transferred to the Human Rights Commission Act.

Property agreements in de facto relationships

159 Section 40A sets at rest any fears that arrangements for the sharing of property made between a man and a woman who are cohabiting as husband and wife, although not legally married to each other, run foul of the old rule that a contract made upon a sexually immoral consideration or for a sexually immoral purpose is against public policy and therefore illegal and unenforceable. It seems unlikely that a court, in the absence of this section, would now come to this conclusion in relation to a property agreement, though it might well have done not many years ago. The section is valuable in putting to rest any residual doubt. It should be brought forward.

160 The Commission has considered whether, now that homosexuality has been decriminalised in New Zealand (Homosexual Law Reform Act 1986), section 40A should be expanded to cover property agreements made between *any* persons who are cohabiting. This would remove the possibility that the property aspects of a cohabitation agreement between a non-heterosexual couple might be held to be illegal. It would also prevent a party who intended to be bound by the terms of such an agreement from subsequently escaping from the obligations by arguing that the agreement was illegal.

161 It can be anticipated that there will be opposition to this suggested extension of section 40A on the grounds that whilst public morality might no longer be outraged by heterosexual cohabitation, it is not so liberal as to sanction non-heterosexual cohabitation, even if this is no longer an appropriate area of concern for the criminal law. The counter to that view is that the proposition is not that the entire cohabitation agreement be saved from illegality, but just those aspects which relate to property.

Question:

Q23 Should section 40A apply to property agreements made between any persons who are co-habiting?

APPORTIONMENTS IN RESPECT OF TIME

162 Sections 144-148 have their origins in the Apportionment Act 1870 which is still in force in England. They are almost identical to the sections in that statute. They provide for rents, annuities, dividends and other periodical payments in the nature of income to accrue from day to day and be apportioned in respect of time. To be apportionable a payment must relate to a period: otherwise how can it accrue from day to day? (*In Re Griffith* (1879) 12 ChD 655).

163 The sections apportion as to time both the right to receive payment and the liability to make payment (*Bishop of Rochester* v *Le Fanu* [1906] 2 Ch 513). They do not, of course, advance the date on which payment is due (*In Re The United Club & Hotel Co Ltd* (1889) 60 LT 665). The apportioned part is payable as soon as the sum of which it forms part becomes due and payable. Persons entitled to an apportionment are given remedies for its recovery.

164 By way of example, assume that A has leased Blackacre to B for $1000 per annum, payable quarterly in arrears on the first days of January, April, July and October. A sells Blackacre to C subject to B's lease, with settlement on

1 February. The Act, and no doubt the contract also, requires that upon settlement A and C must apportion between them (in this case as to one-third to A and two-thirds to C) the rental instalment which B will pay on 1 April. (Contracting out is permissible.)

165 Rent was originally not apportionable at common law. The right to apportion it therefore depends either upon the Property Law Act or upon express agreement. In *Ellis* v *Rowbotham* [1900] 1 QB 740 it was held that rent payable *in advance* fell due and became the absolute property of the landlord on the first day of the rent period and was not apportionable if the lease was lawfully terminated by the landlord for breach during the rent period. Thus the landlord could keep the whole amount received or could sue the former tenant for the whole of the rent for that period. There does not appear to be any sufficient reason to disturb this rule but it could be made clear that, where interests in land, either freehold or leasehold, are changing hands, rent receivable or payable by the owners of those interests is apportionable between vendor and purchaser regardless of whether it is payable in advance. This now has to be dealt with by specific provision in the agreement for sale and purchase.

166 In *Wallace* v *Ross* (1915) 17 GLR 518 Hosking J doubted whether the apportionment provision for "salaries" included a bonus payable to an employee on an annual basis as a percentage of profits. For this reason a reference to "bonus" is suggested for inclusion in the definition of "periodical payments". The word already appears in the definition of "dividends".

Question:

Q24 Should the new Act apply to apportionment of rent in advance as between vendor and purchaser of a reversion or a lease?

DIVISION OR SALE OF CO-OWNED PROPERTY

167 Sections 140-143 concern property owned in a joint tenancy or a tenancy in common. Before the passing of the Partition Acts of 1539 and 1540, co-owners had no right to have their land either partitioned or sold and were thus locked into it until they reached agreement on a method of exit. Those Acts gave a right to a partition. The history is to be found in *Patel* v *Premabhai* [1954] AC 35, 41-42 (PC) and in *Fleming* v *Hargreaves* [1976] 1 NZLR 123 (CA).

168 There was no other remedy in England until the Partition Act 1868, which was copied by an Act of the same name in New Zealand in 1870. The 1870 legislation is the predecessor of sections 140 to 143 of the Property Law Act 1952, though in a different form. The power of the court

to make an order of sale of chattels does not appear on the face of section 143 but has been held to exist (*Hargreaves* v *Fleming* [1975] 1 NZLR 209 (SC)), there having been no appeal on this point.

169 A difficulty with the present sections is the lack of flexibility where a half-owner applies. The court must order either a partition or a sale. It cannot refuse to make any order at all unless the application is by someone with less than a half interest. Where subdivision is impossible because of the requirements of the Local Government Act 1974, the court will often have no choice but to order a sale. Its power to require one co-owner to buy out the other is limited: under section 140(3) it can, upon request of "any party interested", direct that the land be sold unless "the other parties interested or some of them" undertake to purchase the share of the party requesting a sale. The court has no power to make such an order unless the request is made to it. Nor can such an order be made in respect of chattels (*Hargreaves* v *Fleming*).

170 A further difficulty is that the court is not empowered to take into account the sentimental value of the property (*Drinkwater* v *Ratcliffe* (1875) LR 20 Eq 528).

171 Sections 140-142 deal with land and section 143 deals with chattels. There seems to be no good reason why all kinds of property cannot be dealt with under the same provision. The court would have power to take into account the nature of the property.

172 Although the point seems to have been disposed of in the *Fleming* v *Hargreaves* litigation, it would perhaps be helpful to include a subsection stating that the right to a sale or division applies in the case of land registered under the Land Transfer Act.

173 It would be useful if both legal and equitable co-owners could use the section and if it were also to extend to a mortgagee of a co-owner.

Questions:

Q25 **Should the court be given more flexible powers to determine questions of partition or sale between co-owners as follows:**

- **order for sale and division of proceeds**
- **division in specie**
- **one or more co-owner(s) to purchase share of other(s), or sale if this is not done**
- **postponement of sale or division**
- **no order at all?**

Q26 **Should the powers extend to equitable owners and mortgagees?**

PRESCRIPTIVE RIGHTS

174 A prescriptive right is one acquired by use or enjoyment of land during the time and in the manner fixed by law (Hinde McMorland & Sim at para 6.045). Easements and profits à prendre may be created by prescription.

175 There are three ways in which a prescriptive easement or profit may be acquired:

- by operation of the common law prescription rules;
- by the fiction of a lost modern grant; or
- under the Prescription Act 1832 (2 & 3 Will 4, c 71), which remains in force: Imperial Laws Application Act 1988, First Schedule.

176 At common law a right could be acquired by prescription only where user had existed from time immemorial, ie, from 1189. Clearly this rule could have no application in New Zealand.

177 The fiction of the lost modern grant, however, could apply - at least in theory. But it is unlikely that it would be relied upon at the present day.

178 The general effect of the Prescription Act is that a prescriptive easement may be acquired over land which is *not* under the Land Transfer Act 1952 if 20 years uninterrupted user can be proved. Similarly, a prescriptive profit over non Land Transfer land can be acquired by 30 years user. A prescriptive right which has matured before land was brought under the Land Transfer Act prevails against the registered title: section 62(b) of the Land Transfer Act 1952. But, subject to that, a right cannot be acquired by prescription against Land Transfer land.

179 So far as Crown land under the Land Act 1948 is concerned, section 172 of that statute provides that no right-of-way shall by reason only of user be presumed or allowed to be asserted or established as against the Crown or as against any person or body holding lands for any public work or in trust for any public purpose or as against any state enterprise under the State-Owned Enterprises Act 1986. It seems unlikely that any profit à prendre currently enjoyed would have matured under the Prescription Act against the Crown. Rights in relation to Maori land can generally be acquired only in terms of the Maori Affairs Act 1953.

180 Therefore the rules concerning prescription relate only to deeds system land which has not been brought under the Land Transfer Act. Very little of this remains. It was the view of PLERC in its *Report on Imperial Laws Application Bill*

(1985), para 6.6, that prescriptive rights should be abolished in New Zealand. At para 6.4 the Committee said:

> Probably its main continuing operation is in the rare cases of small pieces of land, eg, small access lanes in closely built urban areas, which by oversight have not been brought under the Land Transfer Act and to which in any event the adjoining registered proprietors may well be able to obtain title under Part IV of the Land Transfer Act 1952.

181 Rights of this latter kind are all no doubt fully matured in the sense that they have already existed for over 20 years. Moreover, it is possible that an essential ingredient of maturity is the bringing of an action and that no matter how long the use has been enjoyed, no title is acquired under the 1832 statute until proceedings are initiated: compare *Colls v Home and Colonial Stores Ltd* [1904] AC 179, 189-190, which is to this effect, with the decision of the Court of Appeal in *New Zealand Loan & Mercantile Agency Co Ltd v Corporation of Wellington* (1890) 9 NZLR 10, 22-23 to the contrary. They are discussed in *NZ Torrens System Centennial Essays* 162 at 172-174 by Professor Brookfield in his essay on "Prescription and Adverse Possession".

182 The Law Commission's provisional opinion is that prescriptive rights of all kinds should be abolished in New Zealand and that there is no good reason for allowing the maturity of any further rights: in all probability none are presently maturing anyway. In this respect our approach is the same as that which the Commission adopted in relation to the parallel doctrine of adverse possession in its report on *Limitation Defences in Civil Proceedings* (NZLC R6).

183 However, presently section 7 of the Limitation Act 1950 prevents actions being brought for the recovery of land after the expiry of 60 years (in the case of the Crown) and 12 years (in the case of any person other than the Crown). The Law Commission's draft Limitation Defences Act recognised that this was not compatible with its proposal to abolish adverse possession and therefore provided that a limitation defence could not be raised in the case of "a claim for recovery of possession of land when the person entitled to possession has been dispossessed in circumstances amounting to trespass" (see clause 17 of the Bill which is contained in the Report). If legislation abolishing prescriptive title is passed before a new Limitation Defences Act comes into force, abolition will need to be accompanied by an appropriate provision along similar lines.

Questions:

Q27 Should prescriptive claims continue to be allowed?

Q28 If not, should any present claims be enabled to mature?

V
AGREEMENTS FOR SALE AND PURCHASE

184 This chapter contains discussions of some unrelated matters concerning the law of vendor and purchaser.

VENDORS' LIENS

185 Were it not for section 28 of the Property Law Act, a vendor of land would have an equitable lien for any unpaid part of the purchase price on the land which is the subject matter of the sale and purchase. The lien arises by operation of law at the moment when the contract of sale is signed and so is not registrable as a charge. It binds both the purchaser and those claiming through the purchaser but is, of course, liable to be defeated by registration under the Land Transfer Act by a bona fide third party who gives value.

186 Section 28, which has been in the Property Law Act since the Conveyancing Ordinance of 1842, declares that no vendor of any land shall have any equitable lien thereon by reason of the non-payment of purchase money. We see no reason to reverse this. For all practical purposes it does away with vendors' liens in New Zealand. However, as is pointed out in 42 *Halsbury's Laws of England* (4 ed) at para 193, the equitable lien begins its life as a common law (legal) lien and retains that status while the vendor retains possession of the title deeds. Once they leave the vendor's possession, as they would normally do on settlement, the lien is converted into an equitable one. Although section 28 does not take away the legal lien, it is not easy to discern any practical function for it. A vendor is, before settlement, adequately protected by his or her legal ownership and by the fact that the purchaser has no right in terms of the contract to ask for delivery of title documents. The legal lien therefore appears to serve no purpose. The Commission has formed the view that it also should be abolished.

Question:

Q29 Should vendors' legal liens be abolished?

RIGHT OF PURCHASER IN POSSESSION TO RELIEF AFTER TERMINATION OF AGREEMENT

187 Section 50 applies the provisions of the Act in section 118 for relief against forfeiture of a lease to a "right or option to purchase any land" where the purchaser is in possession "as if any right of rescission or determination exerciseable by a vendor were a right of re-entry or forfeiture by a lessor". This has been held to include not merely a situation where someone has an option to purchase but also one where there is an existing agreement for sale and purchase.

188 The language of section 50 now seems rather old-fashioned. "[R]escission or determination" is also inappropriate in the case of an option, where the would-be purchaser, who has failed to comply with a condition of exercise, simply loses the right to do so: it is not a case of rescission by the vendor.

189 In the context of section 50, "possession" has been held to mean legal possession or the right to legal possession (*Woods* v *Tomlinson* [1964] NZLR 399). This could be stated in a replacement section.

190 In practice, the only situations in which someone who is buying or intending to buy land is in possession are either where there is an agreement for sale and purchase, or where that person is a lessee or licensee and has a right of purchase containing a compulsory or optional purchasing clause. The latter situation falls under the Law Commission's proposed amendments to sections 120 and 121. It is suggested (at para 563) that section 120 should apply where there is a licensee in possession and should also apply whether or not the right of purchase is contained in the lease or licence. With that reform of section 120, it would seem unnecessary to preserve in section 50 any right of relief for an option holder. Section 50 can then be confined to an existing agreement for sale and purchase where the purchaser is in possession. (There would be an overlap where a lease contained a compulsory purchase clause but this will not matter if sections 50 and 120 are consistent in relation to relief.)

191 The Commission envisages that a new section 50 would stand on its own feet (ie, without cross-reference to sections 118 and 120-121) and would provide that where a purchaser is in (or has the right to) legal possession the vendor must not cancel the agreement by reason of any breach unless:

- the breach is subsisting; and
- the vendor has given 12 working days' notice specifying the breach and requiring it to be remedied; and
- the breach has not been remedied.

The period of 12 working days is that found in the agreement form approved by the Real Estate Institute and the New Zealand Law Society. It was thought to be adequate by Fisher J in *Bidmead* v *District Land Registrar* (unreported, High Court, Hamilton, 20 July 1990, CP 287/89). The purchaser would have a right to relief as at present but application would have to be made within three months after cancellation. The notice given by the vendor would be required to draw attention to the right to apply for relief and to the time limit. Contracting out would not be permitted.

192 Unlike the case of a breach of lease, governed by section 118, it seems sufficient to refer to the remedying of the breach. Normally this will involve the payment of money. If a situation arises in which a breach cannot physically be remedied, but it is appropriate that the vendor accept compensation in lieu, the court can surely take that into account upon an application for relief.

193 It also seems desirable to remove the equitable jurisdiction of the court, recently enunciated by the High Court of Australia in *Legione* v *Hateley* (1983) 152 CLR 406 but doubted in New Zealand in *Location Properties Ltd* v *G H Lincoln Properties Ltd* [1988] 1 NZLR 307. This could produce considerable uncertainty and would probably never be exercised in favour of a purchaser who had not been in possession. Removal of the equitable jurisdiction to relieve *against cancellation* would not affect the jurisdiction of the court to relieve against forfeiture *of instalments of purchase price. Legione* v *Hateley* concerned forfeiture of the purchaser's equitable interest in the land, as does section 50.

194 Section 152, which provides for a mandatory means of service of notices, presently does not refer to section 50 since a purchaser's rights under that section are exercised under section 118, to which section 152 does refer. The new section 152 will need to refer directly to section 50.

Questions:

Q30 **Should section 50 be confined to agreements, with relief against loss of options held by persons in possession being dealt with in sections 120 and 121?**

Q31 **Is the scheme of the section set out in para 191 appropriate?**

Q32 **Should the equitable jurisdiction be excluded?**

RECOVERY OF PURCHASER'S DEPOSIT WHERE VENDOR IS REFUSED SPECIFIC PERFORMANCE

195 Occasionally circumstances arise in a contract for the sale of land where, because of the view it takes of the conduct of the vendor, the court may refuse enforcement by way of a decree of specific performance at the suit of the vendor without finding any breach of contract on the part of the vendor. For example, there may appear on the vendor's certificate of title a reasonably serious blemish but one which is within the terms of the requisitions clause. The vendor may have failed to point this out to the purchaser before the contract is signed and the purchaser may have lost the right to requisition by neglecting to put in a requisition within the time limited by the requisitions clause. In the exercise of its discretion the court may decide that the purchaser should not be forced to take the property subject to

that blemish; but the contract will remain on foot and the vendor may keep the deposit and pursue the purchaser in an action for damages if the deposit is insufficient to cover losses on resale.

196 A further example is a failure by the vendor to point out a defect in quality which the vendor has no legal duty to disclose but of which the vendor knows the purchaser is ignorant. Examples of situations in which a purchaser was unable to recover a deposit after a vendor had been refused specific performance are found in *Beyfus* v *Lodge* [1925] Ch 350, *Summers* v *Cocks* (1927) 40 CLR 321 (where the possibility of a damages action by the vendor is mentioned in the dissenting judgment of Higgins J at 329-330) and *Faruqi* v *English Real Estates Ltd* [1979] 1 WLR 963.

197 However, in the last of these cases the purchaser in fact recovered his deposit by virtue of section 49(2) of the Law of Property Act 1925 (UK) which reads:

> Where the court refuses to grant specific performance of a contract, or in any action for the return of a deposit, the court may, if it thinks fit, order the repayment of any deposit.

Subsection (3) states that the section applies "to a contract for the sale or exchange of any interest in land".

198 It has been held by the English Court of Appeal in *Universal Corporation* v *Five Ways Properties Ltd* [1979] 1 All ER 552 that the court has under section 49(2) an unqualified discretion to order repayment of a deposit where the justice of the case so requires it as being the fairest course between the parties, subject only to the discretion being exercised judicially and with regard to all relevant considerations, including the terms of the contract.

199 In Australia the section has been applied - and deposits ordered to be returned - after a purchaser has defaulted for a reason unconnected with any problem with the vendor's title and where it appears that the vendor could successfully have sought a decree of specific performance (*Wilson* v *Kingsgate Mining Industries Pty Ltd* [1973] 2 NSWLR 713 and *Blacktown City Council* v *Fitzgerald* (1991) ANZ Conv R 94). The Law Commission does not commend a reform which allows the purchaser to claim back the deposit in such circumstances.

200 Although the section does not expressly state that the contract is at an end, so that consequentially the vendor is unable to pursue a damages action, that is the practical effect (*Schindler* v *Pigault* (1975) 30 P & CR 328). The situation created by the section, if the court decides to order a return of the deposit, is rather unusual, for the purchaser may have no right to cancel the contract, the vendor not being in substantial (or, sometimes, any) breach of the contract. The jurisdiction given by the section is clearly equitable in character, as was recognised by Walton J in

Faruqi v *English Real Estates Ltd.* Section 49(2) is, in effect, intended to enable the court in its equitable jurisdiction not merely to deny specific performance to the vendor but also to bring the contract to an end.

201 Section 49(2) of the Property Law Act 1958 of Victoria is in the same terms as the English provision but in some Australian states the approach is slightly different. Section 69 of the Property Law Act 1974-1986 of Queensland limits the circumstance in which the purchaser can recover a deposit to one where a decree of specific performance "would not be enforced against the purchaser by the court by reason of a defect in or doubt as to the vendor's title, but such defect or doubt does not entitle the purchaser to rescind the contract". In that circumstance the purchaser has the right to recover the deposit and any instalments under the contract - the court has no discretion - and is expressly "relieved from all liability under the contract". Although, once again, it is not directly stated that the contract is at an end, that must be the effect of the provision. However, the section does not apply if the contract disclosed the defect or doubt and contained a stipulation precluding the purchaser from objecting to it.

202 The Queensland section also gives the purchaser the right to recover the expenses of investigating the title if the defect or doubt was not disclosed by the contract and was one which was known or ought to have been known to the vendor at the date of the contract.

203 Section 55 of the New South Wales Conveyancing Act 1919 contains equivalents of both the English/Victorian and the Queensland sections. It expressly enables the court to award interest on the deposit which is ordered to be repaid but does not extend to an instalment which is not a deposit. The New South Wales provision also enables the court to declare and enforce a lien in respect of the recoverable deposit on the property which is the subject matter of the contract.

204 It does not appear from the case law that any of the various sections has been used on a large number of occasions. Indeed, some of the cases in which section 49(2) is mentioned as a basis for recovery by the purchaser of the deposit have in fact concerned situations in which the purchaser would have been entitled to cancel in the orthodox way and thereafter to recover the deposit because the contract had come to an end.

205 In New Zealand the law relating to misrepresentation has been liberalised in the Contractual Remedies Act 1979 and, in relation to business contracts, purchasers have extensive rights under the Fair Trading Act 1986 where there has been deceptive or misleading conduct by vendors acting in the course of trade. For these reasons we conclude that if New Zealand were to adopt a version of the section, it would be used relatively infrequently. Nevertheless, the examples given above provide instances in which a section which gave the court discretion to order return of the deposit might be

useful. We do not presently favour a mandatory requirement or limiting the circumstances in which the section would operate to those concerning title defects. Termination of the contract may be appropriate where, for example, there has been a failure to disclose in circumstances where there has been no misrepresentation and the Fair Trading Act is inapplicable. However, the Law Commission believes that any new section should apply only where the vendor has been or would be refused a decree of specific performance.

Questions:

Q33 Should the court be given discretionary power to order return of a deposit where it refuses (or would refuse) to grant specific performance to a vendor but the purchaser is not entitled to cancel?

Q34 How should the power be defined?

WAIVER OF CONTINGENT CONDITION

206 The law governing the ability or otherwise of purchasers to waive contingent conditions in contracts for the sale and purchase of property seems to the Law Commission to be unsatisfactory. It is well established that a contingent condition can be waived unilaterally only when it is inserted into the contract for the benefit of the party who waives it. It is then a power or right vested by the contract in that party alone (*Heron Garage Properties Ltd* v *Moss* (1974) 1 WLR 148, approved by the New Zealand Court of Appeal in *Moreton* v *Montrose Ltd* [1986] 2 NZLR 496). Thus where the fulfilment of the condition may be of substantial benefit to both parties (such as a town planning condition in circumstances where the vendor owns adjoining land), the condition can be *treated* as being fulfilled and the contract unconditional only when both parties so agree.

207 But normally a contingent condition will specify the date by which it must be fulfilled (the condition date) and will also expressly state that if it is not fulfilled by the condition date, *either party* may cancel the contract by notice in writing to the other. It would be strange if this were not so - if only the party with the benefit of the substance of the condition were able to terminate it - for otherwise one party would have no means of bringing the contract to an end and it could be continued for an indefinite period despite failure of the condition. Presumably in those circumstances the condition could be fulfilled out of time. If so, the only significance of the condition date would be that it gave one party the ability to terminate for non-fulfilment after that date had passed. However, this point may be of little importance since in practice conditions are not drawn in this manner.

208 The courts both in New Zealand and elsewhere in the Commonwealth have not drawn any distinction between the

benefit of the substance of the condition and the procedural benefit conferred on both parties by the right of termination. They have regarded the existence of the right in both parties as an indication that the condition is not for the sole benefit of a party who alone benefits from the substance of the condition. So a condition in an agreement for sale and purchase of land where the purchaser is to raise finance of a stated sum or is to sell his or her existing property - either circumstance being plainly for the sole benefit of the purchaser in its substance - would apparently be regarded by the courts as being incapable of waiver by the purchaser if *either* vendor or purchaser has a right of cancellation for non-fulfilment by the condition date. Hence the dicta in *Moreton* v *Montrose Ltd*:

> In short, when it is expressly agreed that in a certain event the contract shall be void or voidable by either party, I think that as a matter of interpretation such a clause is normally for the benefit of both and cannot be waived by one only. (Cooke J at 504)

And:

> Where the contract gives an express right of rescission to one or both parties on failure of the condition, that right must prevail and cannot be taken away by the other party seeking to waive it. (Casey J at 511)

209 It was suggested by Cooke J at 504 that to construe such a condition as being for the benefit of one party only might be "subversive of certainty" but, in the view of the Commission, upon closer examination this is debatable. The purpose of giving a right of cancellation to both parties is that, when the condition date has passed, each has the certainty of knowing whether the contract is to proceed. It would be entirely unsatisfactory if one party had simply to wait and see. It does not seem that certainty of this kind would be subverted by allowing a party with the substantive benefit of the condition to give notice of waiver making the contract unconditional.

210 It is noteworthy that the standard agreement for sale and purchase form approved by the Real Estate Institute of New Zealand Inc and the New Zealand Law Society endeavours to counter the result in *Moreton* v *Montrose Ltd*, seen as unsatisfactory in practical terms, by expressly permitting waiver of conditions which are for the substantive benefit of one party. We are not aware of any criticism of the manner in which such a clause operates and believe it reflects what the general law should be. The Court of Appeal has found the clause to be effective in its own terms (*Hawker* v *Vickers* [1991] 1 NZLR 399).

211 We accordingly propose the inclusion in the proposed new Property Law Act of a provision upon the following lines:

> A contingent condition in a contract for the sale and purchase of property:

(a) may be waived by any party or parties to that contract for whose exclusive benefit that condition has been included in the contract;

(b) may be exclusively for the benefit of a party not withstanding that any other party has the right to cancel the contract if the condition is not satisfied by a time stipulated in the contract or within a reasonable time.

Question:

Q35 Should a provision to this effect be included in the new Act?

MORTGAGES BY VENDORS OF LAND

212 A purchaser of land holding under an agreement for sale and purchase cannot object to the presence of a mortgage on the vendor's title even though the amount secured may exceed the price and even though the mortgage may become repayable because of the existence of the agreement for sale or because the maturity date is earlier than the settlement date under the agreement. It appears that it is only where the property is in jeopardy because of the vendor's mortgage default that the purchaser has the ability to pay the mortgagee the amount needed to avert a sale and to set off the amount paid against the balance owing under the agreement. Even then, no case directly supports this last statement.

213 Moreover, there is nothing to prevent a vendor from mortgaging the property between the date of contract and the date of settlement provided the vendor makes good title on settlement (*Burges* v *Williams* (1912) 15 CLR 504).

214 While there may be no complete cure for these problems, there may be useful reform in three ways (which are not intended to compromise the paramountcy of the Land Transfer Act register and would apply subject to that Act):

- including a compulsory term in an agreement of the sale of land prohibiting the raising of new mortgages to the extent that amounts secured over the property will exceed (say) 90 per cent of the outstanding purchase price;

- enabling the purchaser to pay to a mortgagee the amount of any default under the mortgage, with that payment going in reduction of the purchase price and, to the extent it exceeds it, being recoverable from the vendor with interest; and

- allowing the purchaser to withhold instalments of purchase price where amounts secured by mortgages over the property already exceed, or would upon the making of any further payment exceed, the

unpaid purchase price, such withholding to continue until the vendor arranges for the instalments to be received by the mortgagee(s) in reduction of the mortgage(s) and for the mortgagee(s) to acknowledge in writing the availability of discharge(s) of mortgage when the entire purchase price has been paid.

Subpurchases

215 The situation is complicated by the possibility that there may be more than one mortgage and the further possibility that the agreement is a subpurchase and any mortgage may have been given by the registered proprietor, rather than by the vendor.

216 The first of the suggested reforms may be less effective in circumstances where the purchaser holds by a subpurchase agreement since, although the vendor will have similar rights under the head agreement, the vendor may neglect to enforce them. But it seems to be unreasonable to go further and impose upon the original vendor limitations in its ability to raise mortgage moneys, these limitations being related to a subpurchase for which it has no responsibility.

217 However, the second and third proposals are designed to give the subpurchaser some protection by enabling it to make payment to the original vendor's mortgagee and to withhold payments under the subpurchase agreement until the original vendor's mortgagee has agreed to accept payment and to make available a discharge when the full price under the subpurchase agreement has been paid. In this circumstance, the intermediate party (the vendor under the subpurchase agreement) may encounter difficulties in making arrangements with the original vendor's mortgagee. This should, we think, be a risk undertaken by anyone who elects to sell by subpurchase agreement, ie, before taking title to the property. The risk should not fall on the subpurchaser. Furthermore, the existing law appears to be that a subpurchaser is entitled to ask its vendor to obtain an assurance from the registered proprietor of consent to the subpurchase and is further entitled to an assurance from its vendor that there will be no impediment to the availability of title on settlement (*Jenkinson* v *Krchnavy* [1979] 1 NZLR 613).

Question:

Q36 Should the law relating to vendor mortgages be reformed in all or any of the ways described in para 214?

TENDER OF PAYMENT BY BANK CHEQUE

218 A payment or tender of money must be made in legal currency (9 *Halsbury's Laws of England* (4 ed) para 524). In New Zealand every banknote issued or deemed to be issued under the Reserve Bank of New Zealand Act 1989 is legal tender for

the amount expressed in the note and coins issued or deemed to be issued under the Act are legal tender for payment of limited sums (section 27, Reserve Bank of New Zealand Act 1989).

219 In order to demonstrate readiness, willingness and ability to settle a transaction under which property is being bought and sold it is prudent to tender to the vendor the amount due on settlement. This can strictly be done only by tender in compliance with section 27 which, for practical purposes, means tender of banknotes. The larger the transaction, the more difficult this may be to arrange and the more danger there will be of robbery or other loss. Vendors and their solicitors will usually dispense with the need for tender of banknotes and will treat tender of a bank cheque as sufficient. But the law does not require this: a bank cheque is not legal tender (*Commonwealth Trading Bank of Australia* v *Sidney Raper Pty Ltd* [1975] 2 NSWLR 227, 233). Compare however, the dictum of Somers J in *Henderson* v *Ross* [1981] 1 NZLR 417, 433 that he would not wish it to be supposed that he necessarily accepted that as between vendor and purchaser only banknotes and coin are proper tender and that "[t]he essence of the matter may well be that the vendor has the certainty of actual receipt".

220 Although it is likely that the courts will strive to avoid visiting upon a purchaser whose tender does not comply with the Reserve Bank of New Zealand Act the consequences of having failed to make legal tender and may find that tender of a bank cheque or some other form of tender is in the circumstances sufficient evidence of readiness, willingness and ability to settle, it does not seem to the Commission that the existing law on this subject is in a satisfactory state. It is also uncertain whether the courts would at the present day treat tender of a bank cheque accompanying exercise of an option as sufficient compliance with the condition of exercise that it be accompanied by "payment". In *Plimmer* v *O'Neill* [1937] NZLR 950 the court did not regard tender of a cheque drawn on a substantial public company as sufficient to meet a condition of this kind. Consequently, the option was not validly exercised.

221 However, although the law could simply be changed so that bank cheques (ie, those drawn by the holder of a banking licence under the Reserve Bank of New Zealand Act 1989) were treated as the equivalent of legal tender, there is good reason why statute should not declare this. Although the Reserve Bank requires certain criteria to be met by applicants for banking licences and exercises prudential supervision over the holders of licences, there are numerous licence holders and it cannot be assumed that every holder will at all times be sufficiently substantial that it would be safe to deem its obligation to pay on demand to be the equivalent of cash. We understand that it would not be the wish of the bankers themselves that this should be so. It is conceivable that at some future time there may be very reasonable reluctance on the part of bankers and others to rely upon cheques issued by an institution merely because it continues to hold a licence under the 1989 Act.

222 Section 61 of the Property Law Act 1974-1986 of Queensland provides, in relation to contracts for the sale of land, that there shall be implied a term that payment or tender of any moneys payable pursuant to the contract may be made by cheque drawn by any bank. For the reason already given, we do not think that this model should be adopted in New Zealand. However, we suggest that, if it is thought that reform is needed, it could be as follows:

- in the absence of proof to the contrary it would be presumed that where for the purpose of paying any sum in relation to a contract for the sale or other disposition of property, one person tendered to another person a bank cheque in the amount of that sum, the person tendering was ready, willing and able to pay that sum;

- no person (other than the bank itself) would be permitted to cause a bank cheque to be stopped after it has been delivered to the payee or any endorsee where that person has reason to believe that payment of the cheque is or will be relied upon by the payee or endorsee; and

- "bank cheque" would be defined as a cheque drawn by the holder of a banking licence.

223 It is not intended that any restriction be placed upon the discretion of a bank to stop its own cheque. However, in practical terms, amendments outlined above might make it easier for a bank, in dealing with its customer, to decline to stop a cheque drawn at the request of that customer without having the cheque re-delivered to it. The Commission understands that in practice banks are very cautious about stopping their cheques, particularly where they have reason to believe that they may have been used by way of payment.

224 Parties to transactions would remain free to stipulate in their contracts the manner in which payment is to be made. In larger transactions it is not uncommon for the parties to arrange a direct bank credit or transfer, so that no cheque is delivered on settlement. Such a practice might well continue. However, our proposal would, we think, ensure that it was unnecessary for purchasers to arm themselves with banknotes before attempting a settlement, and would not cause difficulty for a vendor except in the unusual combination of circumstances where:

- the purchaser did not wish to proceed (and was therefore going through the motions of tendering);

- the vendor was genuinely concerned about the solvency of the bank whose cheque was being tendered; and

- time was of the essence.

If the vendor refused to accept the bank cheque and the bank collapsed, the presumption of ability to pay would be rebutted. If the purchaser did not want to withdraw from the transaction, we envisage that the parties would by negotiation make arrangements for the manner of payment.

225 The suggested reform may also assist a person seeking to exercise an option, although it would still be possible for a reluctant vendor to argue that tender of a bank cheque, while it might be evidence of readiness, willingness and ability to pay, was not actual payment. However, we would hope that the New Zealand courts would be encouraged to depart from *Plimmer* v *O'Neill* by construing the obligation to make payment as being an obligation to tender a cheque which the tenderer could not lawfully cause to be stopped, ie, a bank cheque. They might follow the lead of Brandon J in *The Brimnes* [1973] 1 WLR 386, 400 who thought that "cash must be interpreted against the background of modern commercial practice" and "cannot mean only payment in dollar bills or other legal tender".

Questions:

Q37 Should bank cheques be presumed to be legal tender?

Q38 Should a new Property Law Act contain provisions, relating to property transactions, as suggested in para 222?

VI
ASSIGNMENTS OF THINGS IN ACTION

226 Section 130(1) provides as follows:

> **Any absolute assignment by writing under the hand of the assignor (not purporting to be by way of charge only) of any debt or other legal or equitable thing in action, of which express notice in writing has been given to the debtor, trustee, or other person from whom the assignor would have been entitled to receive or claim that debt or thing in action, shall be and be deemed to have been effectual in law (subject to all equities that would have been entitled to priority over the right of the assignee if this Act had not been passed) to pass and transfer the legal or equitable right to that debt or thing in action from the date of the notice, and all legal or equitable and other remedies for the same, and the power to give a good discharge for the same, without the concurrence of the assignor.**

227 The section is largely but not entirely procedural. Assignments of both legal and equitable interests in choses (or things) in action can still be made outside the section. A thing which is not assignable outside the section (such as a bare right of litigation) does not become assignable merely because the procedure prescribed by the section is followed.

228 Choses in action are of two kinds: those that can be sued for at common law (legal choses) and those which are protected only in equity (choses in equity). Examples of the latter are beneficial interests under trusts and partnership interests. Outside of the statute choses in equity can be transferred only by assignments in equity. However the effect of the statute is to enable choses in equity to be transferred in the same manner as legal choses, though it does not change the nature of the thing transferred. Section 130 states its subject matter as being "any debt or other legal *or equitable* thing in action", though the specific reference to equitable things in action does not give the section greater width than its equivalent in England and the Australian jurisdictions. Reference in the section to a "trustee" is in itself sufficient indication that the section extends to equitable choses (*New Zealand Loan and Mercantile Agency Co Ltd* v *Ellen Mitchell* (1906) 26 NZLR 433).

229 An assignment which is made in a form complying with the section (ie, an absolute assignment in writing signed by the assignor) is valid and complete as between the parties before any notice is given, but until the giving of the notice it is merely an equitable assignment (*Gorringe* v *Irwell India Rubber and Gutta Percha Works* (1886) 34 ChD 128 and *Holt* v *Heatherfield Trust Ltd* [1942] 2 KB 1). Once the notice is given the assignment becomes a legal assignment ("effectual in law") by which the assignor's rights are vested in the assignee - but subject to equities including, in the case of

an assignment by way of mortgage, the equity of redemption. If an assignment complies with the section the assignee can sue the debtor without joining the assignor in the proceedings. The effect of the notice as against the debtor is to require the debtor to pay the assignee rather than the assignor. Its effect as against other claimants is to fix the priority amongst assignees, which goes to the assignee who first gives notice to the debtor (*Dearle* v *Hall* (1828) 3 Russ 1; 38 ER 475). The rule in *Dearle* v *Hall* is not, however, dependent on the section: it applies also in the case of assignments outside the section.

ASSIGNMENTS WITHIN THE SECTION

230 The section is confined to "absolute" assignments. There must be an existing property interest (not merely an anticipation of a property interest which will arise in the future) and that interest must be transferred to the assignee, rather than merely charged in favour of the assignee. The section itself says that an assignment by way of charge does not comply. However, an assignment by way of legal mortgage vests full title in the assignee (albeit subject to an equity of redemption) and so falls within the section (*Tancred* v *Delagoa Bay and East Africa Railway Co* (1889) 23 QBD 239).

231 The requirement that the assignment be "absolute" also prevents a conditional assignment or one for a limited period coming within the section (see respectively *Re Williams* [1917] 1 Ch 1 and *Durham Bros* v *Robertson* [1898] 1 QB 765, 773).

232 An assignment of part of a debt is not within the section. A debt is not capable, without the consent of the debtor, of being broken up and sued for piecemeal in a court of law. But an attempt to assign part of a debt is effective in equity. It is sometimes said to create a charge on the assignor's interest but the word "charge" means no more than that the assignee has an equitable right against the fund. Whether there is a true charge (of a kind requiring registration under the Companies Act or the Chattels Transfer Act) depends upon whether the assignment is absolute or by way of hypothecation (*Ashby Warner & Co* v *Simmons* (1936) 106 LJKB 127 at 132-133. See also *Sandford* v *D V Building & Constructions Co Pty Ltd* [1963] VR 137). Because an assignment of part of a debt is outside section 130 the assignor must be a party to the proceedings for enforcement of the assignee's interest. The assignee is regarded as a creditor of the debtor in equity. The Law Commission suggests that the new Act could provide that a part of a debt or other legal or equitable thing in action may be assigned absolutely but that the assignee may not recover judgment for that part unless every person entitled to any part of it is joined in the proceedings. This reform would not improve the procedure which must be followed but would enable the assignment to be a legal assignment, as well as making the procedure explicit.

CONSIDERATION

233 Although the matter has not been determined in any of the higher courts, it seems now to be fairly well established

that it is not a requirement of section 130 that consideration be given by the assignee (see *Re Westerton* [1919] 2 Ch 104 and the exposition of Windeyer J in *Norman* v *Federal Commissioner of Taxation* (1963) 109 CLR 9, 28, in which Dixon CJ concurred). The difficulty over an attempt to assign a future debt also comes down to the question of consideration. Property can be gifted by a conveyance which has immediate effect. Because a future debt is not property, an attempt to assign it amounts to no more than an agreement to do so. An agreement to do an act in the future, like any other species of ordinary contract, requires consideration. The position was summarised in *Williams* v *Commissioner of Inland Revenue* [1965] NZLR 395, 399 in the joint judgment of North P and Turner J as follows:

> But while equity will recognise a voluntary assignment of an existing equitable interest, it will refuse to recognise in favour of a volunteer an assignment of an interest, either legal or equitable, not existing at the date of the assignment, but to arise in the future. Not yet existing such property cannot be owned, and what may not be owned may not be effectively assigned. If not effectively assigned, it is made the subject of an agreement to assign it. Such an agreement may be good in equity, and become effective upon the property coming into existence; but if, and only if, the agreement is made for consideration, for equity will not assist a volunteer. (at 399)

234 And as Windeyer J commented in *Norman* v *Federal Commissioner of Taxation*:

> The distinction is critical, for consideration is always necessary to attract the support of equity to a transaction that is a contract rather than a conveyance. (at 31)

235 This difficulty could be overcome, and assignments of future debts or other choses brought within the section, if it was specifically provided that the future debts or other choses were capable of assignment with immediate effect notwithstanding their lack of present existence as property. The rule that consideration is unnecessary for an assignment with immediate effect could be extended to these species of future property without interfering with the doctrine of consideration in contract law.

236 This would, however, create an exception to the general rule that future property can be assigned only through the operation of the equitable doctrine of part performance which is available only when consideration is given. Should there be an exception in the case of future debts? A justification may be that, as proceeds, they are often assigned along with present property of the assignor. Whether or not this exception is created the section should, we think, confirm that consideration is not necessary for an absolute assignment of a chose in action with immediate effect.

EXECUTION BY ASSIGNOR'S AGENT

237 A further clarification of the dealings between the assignor and the assignee would be an express statement that an assignor may execute through an authorised agent. As section 130 is intended to reduce the formality attendant upon assignments of things in action, it seems inappropriate to require that the agent be authorised in writing. Equitable interests in land can, of course, be created by a writing signed by an agent who has been orally authorised. (Compare section 49A(1) in relation to the creation of legal interests in land.)

NOTICE TO DEBTOR

238 We turn now to the question of the notice which must be given to the debtor. Section 130 requires the notice to be in writing, which is not the case outside the statute, where any form of notice sufficient to bring the assignment to the attention of the debtor is enough (*Magee* v *UDC Finance Ltd* [1983] NZLR 438 (CA)). The notice can be given at any time (*Bateman* v *Hunt* [1904] 2 KB 530) and is effective to pass the rights of the assignor to the assignee as from the date of the notice, ie, when it is received by the debtor (*Holt* v *Heatherfield Trust Ltd*).

239 The requirements for giving notice are relatively formal. "Given" has been interpreted as having the same meaning as "served" in section 152. It was held in *Smith* v *Corry & Co* (1909) 28 NZLR 672 that to bind the debtor the assignee must prove either actual receipt or that the notice was served by a registered letter which was not returned. It was held to be insufficient to prove that an ordinary letter duly addressed and posted was not returned, if that letter had not been registered. There have been some changes to the wording of both sections since this case but it still seems to be applicable. Certainly, it would be dangerous to assume the contrary. At paras 658 to 665 we propose changes to section 152, in part as a consequence of the repeal of the Post Office Regulations which established registered mail.

240 Few problems seem to have been caused outside the statute by the giving of oral notices and, if it is thought desirable to bring as many assignments as possible within the protection of the statute, the requirement for the notice to be in writing could well be dispensed with. If a debtor can reasonably feel uncertain whether there has been an assignment, it is always possible for the debtor to seek confirmation in written form. In a case of such uncertainty it would often be found that there had been no *express* oral notice.

241 There is no requirement that the notice to the debtor be given by any particular person. Obviously it could be given by the assignor but it can equally be given by the assignee (Windeyer J at 29 of *Norman* v *Federal Commissioner of Taxation*) or, it would seem, by a third party.

242 A further possible reform of the section would be to make it clear that notice can be given to an authorised agent of the debtor. The risk of proving the authorisation would fall on the person giving notice. It seems that this is already the position (see generally *Magee* v *UDC Finance Ltd*, in which the Court of Appeal, while dealing with the case on the basis that there had been an effective assignment in equity where notice was given to an agent, nevertheless seemed to be of the view that the position would have been the same under the statute).

HARMONISATION WITH REGISTRATION STATUTES

243 If the Personal Property Securities Act (PPSA), recommended by the Law Commission's Report No 8 is enacted, it must be certain that the proposed replacement for section 130 (and, indeed, the law relating to equitable assignments) is in harmony with it. It must also be in harmony with the other registration statutes. Section 130 covers a wider field than PPSA, for the former deals with outright assignments (assignments by way of sale) as well as assignments which are security interests (legal mortgages of choses in action). Where there is competition between two security interest assignments there could be conflict between PPSA and the rule in *Dearle* v *Hall* (see para 229), since priority under PPSA will be determined by time of registration but priority under *Dearle* v *Hall* depends upon the time of the respective notices to the debtor. A revised version of section 130 should ensure that the debtor is entitled to pay in accordance with the notice which he or she receives, until more than one notice has been received, at which point the entitlement to future payments should be determined by the priority under the registration statute. This part of the section should apply also to assignments which are outside the section in other respects.

244 The problem may, at least in theory, already arise in relation to mortgages registered under the Land Transfer Act, which are choses in action as well as interests in land, and to which the rule in *Dearle* v *Hall* would appear to apply. A registered mortgagee could execute two memoranda of transfer to different transferees. One of those transferees may then, in advance of registration of the transfer, give notice to the mortgagor of the assignment. But the other transferee might proceed to register first and only then give notice. It is thought that if the mortgagor made a payment to the first notice-giver before receiving notice from the registered transferee, the mortgagor would be held to have acted properly. However, the point does not seem to have arisen for consideration. Nevertheless, the problem is an existing one and should be addressed whether or not PPSA is enacted. (The rule in *Dearle* v *Hall* does not apply to an assignment of a beneficial interest in land, but we think should be made to do so. It would be inconvenient if an assignment was made of an interest in a mixture of land and personalty and if different priority rules applied to different parts of the same interest. The rule in England has been extended to dealings with equitable interests in land: section 137, Law of Property Act 1925.)

245 Four situations can be identified:

- If both assignments are by way of sale, PPSA is not relevant (although the Land Transfer Act may be) and the rule in *Dearle* v *Hall* prevails.

- If the first assignment is a sale and the second is a security interest, perfection of the security interest under PPSA is irrelevant. The first to give notice prevails.

- If the first assignment is a security interest and the second is a sale, the second assignee will acquire a legal interest under section 130 upon giving notice to the debtor and, depending upon the circumstances, would take the chose in action free of the security interest unless the security interest had first been registered under PPSA.

- If both assignments are security interests, the order of registration under PPSA governs priority but the debtor requires protection pending receipt of actual notice of those registrations.

246 We do not attempt to explore the full range of possibilities as between the assignees. The present concern is the protection of the debtor, who should be entitled to pay a notice-giver during such period as only one notice has been given. Thereafter the debtor should carry out the simple precaution of searching the PPSA register. If a registration by one or more of the notice-givers is discovered, the debtor should withhold payment until the question of priority has been determined; similarly, in the last of the situations, where both of the assignments are security interests. In that case, however, the determination of priority will be much easier since, after both have given notice, priority as between them will be determined by the order of their registration under PPSA.

247 To deal with this problem the new version of the section could say that registration under any of the registration regimes (PPSA, Land Transfer Act, Shipping and Seamen Act 1952) shall not constitute notice to the debtor until express notice of the assignment has been given to the debtor. Constructive notice, which applies under the Land Transfer Act but not under PPSA, should not be relevant.

Questions:

Q39 Should the section confirm that consideration is required for an assignment within the section?

Q40 Should future choses be capable of assignment under the section?

Q41 **Should part of a debt be capable of assignment under the section?**

Q42 **Should the section provide for the assignor to sign by an agent (who would not need a written appointment)?**

Q43 **Should a notice to a debtor:**

- **be able to be given orally?**
- **be able to be given by anyone?**
- **be able to be given to an agent of the debtor (who would not need a written appointment)?**

Q44 **Should a debtor be affected by anything short of express notice of the assignment?**

VII
VOIDABLE ALIENATIONS

INTENT TO DEFRAUD CREDITORS

248 This chapter deals with what are now called fraudulent conveyances (sections 60 and 61 of the Property Law Act). There is extensive case law on section 60 and its predecessor, the Statute of Elizabeth (13 Eliz I, c 5), which was repealed by the 1952 Act. The section is intended to enable the striking down of conveyances of property executed by a person (including a corporation) who is insolvent, or likely to become so, with the intention of putting the property in question out of reach of all or some of the creditors or in some way hindering the creditors from being able to apply the property in recoupment of the money owing to them. It extends beyond a mere transfer of property to catch, for example, the fettering of property by a lease on terms favourable to the lessee or the sale of a property on terms on which the price is payable on a far distant future date or by instalments spread out over a long period. In these examples the lessor's or vendor's creditors are prejudiced by an inability to sell the property (or the debtor's interest in it) except upon terms which are unfavourable because of the arrangement which has been put in place.

249 Section 60 is not concerned with priority between creditors. That has to be considered under the voidable preference sections of the Insolvency and Companies Acts. Therefore the fact that a creditor is preferred and other creditors are thereby disadvantaged is not in itself a ground for setting aside the transaction under section 60. There must be, in addition to an intent to prefer, a further intent to put the property beyond the reach of at least some of the creditors. That is now called an "intent to defraud" creditors, but the Commission favours the words "intent to prejudice" which appear in the cases. The Australian Law Reform Commission has suggested in its General Insolvency Enquiry Report No 45, para 680, "intention of defeating, delaying or obstructing", but we believe that "prejudice" covers all this ground.

250 It is generally thought that the section strikes only at transactions made by a person who is insolvent at the time, though in some of the cases there are statements suggesting that it might be used where a person not presently insolvent transfers property to relatives or to trustees before embarking on a hazardous venture so that the property will not be available to creditors of that venture when and if it fails. The Commission favours extending the section to catch this situation.

251 The new section could also usefully incorporate a statement of the existing caselaw that a gift of property by an insolvent debtor is deemed to have been made with the intention of prejudicing creditors.

252 Section 60(3) provides that the section "does not extend to any estate or interest in property alienated to a purchaser in good faith not having, at the time of the alienation, notice of the intention to [prejudice] creditors". The Commission thinks that the section should refer to the need for full consideration in this context. Section 172(3) of the Law of Property Act 1925 (UK) uses the expression "valuable consideration". We prefer "adequate consideration in money or money's worth" which should avoid the suggestion that "natural love and affection" or something less than full consideration paid in cash or kind is adequate to protect the transaction. The subsection should also, we think, extend to protect third parties who have acted in good faith, without knowledge of the debtor's intention, and who have given adequate consideration to the debtor or the person from whom they acquired the property in issue.

253 The section does not (but probably should) expressly allow recovery of compensation from a person who has received the benefit of the prejudicial conveyance in circumstances where the property cannot be recovered (eg, where it has been on-sold to a bona fide purchaser in the circumstances just mentioned).

254 Dr McMorland in his article "Alienation with Intent to Defraud Creditors" in (1990) 5 BCB 173-176 has drawn attention to the fact that it is uncertain whether and when a fraudulent conveyance which has been registered under the Land Transfer Act may be set aside. (The Official Assignee may do so pursuant to section 58 of the Insolvency Act 1967, which refers to section 60 of the Property Law Act and overrides the Land Transfer Act: section 58 (1) and (7)). The proposed new section could state that nothing in the Land Transfer Act 1952 shall restrict the operation of the section. This is the language used in section 58(7) and also in section 311A(8) of the Companies Act 1955. But it would need also to contain provisions equivalent to section 58(6) and section 311A(7) denying recovery when there has been an alteration of position or when recovery is otherwise inequitable.

INTENT TO DEFRAUD PURCHASER

255 There seems to be no caselaw on section 61, which makes voidable every voluntary alienation of land made "with intent to defraud a subsequent purchaser". Its genesis was 27 Eliz I, c 4 - an Act against covenous (ie, collusive) and fraudulent conveyances - which was repealed in 1952 and replaced by section 61. The Elizabethan legislation treated every voluntary disposition as being fraudulent so that it could always be struck down by a subsequent purchaser for value. As it was put by the Privy Council in *Ramsay* v *Gilchrist* [1892] AC 412 at 415:

> Where two circumstances were found united, an original voluntary gift to a private person, and then a contrary and inconsistent sale by the author of that gift, the Judges, straining the language of the statute, raised from those circumstances a presumption of the fraudulent intent struck at by the statute.

256 The Privy Council noted that those old decisions might not commend themselves if the matter were new but felt that the court had to adhere to well-established law.

257 Evidently in an attempt to get away from the harsh and artificial rule just described, the present section and its equivalent in the United Kingdom - section 174 of the Law of Property Act 1925 - were developed. Now a voluntary alienation is not voidable at the instance of a subsequent purchaser unless the voluntary alienation was made with intent to defraud the purchaser. Moreover, it is not deemed to have been made with intent to defraud by reason only of the fact that it was not made for valuable consideration or by reason of the occurrence of the subsequent purchase.

258 It is a little difficult to see the purpose of perpetuating this watered-down version of the original rule. Under modern New Zealand conveyancing conditions it is hard to conceive of a situation in which a voluntary alienation could be used as a means of defrauding a subsequent purchaser and, even if that did occur, would it really be necessary to rely upon the statute before a court could deprive the volunteer of the benefit of the transferor's fraud? A party to a fraud cannot take advantage of it; nor, it is thought, can a volunteer. On the other hand, an innocent volunteer would get an indefeasible title under the Land Transfer Act if *Bogdanovic* v *Koteff* (1988) 12 NSWLR 472 is followed in New Zealand. If the section is re-enacted it will therefore need to include a clause overriding that Act.

Questions:

Q45 **Should section 60 be made applicable to a person who divests property before embarking on a hazardous venture with the intention by so doing to prejudice creditors of the venture?**

Q46 **Should section 60(3) require that adequate consideration have been given by the alienee?**

Q47 **Should section 60(3) extend to third parties?**

Q48 **Should section 60 allow recovery of compensation where the property itself cannot be recovered?**

Q49 **Should section 60 override the Land Transfer Act?**

Q50 **Is there any purpose in re-enacting a version of section 61?**

VIII
COVENANTS

259 Part V of the Property Law Act (sections 63 to 71) contains a series of sections dealing with covenants and powers. While the drafting requires some modernisation, the Commission has not to date concluded that changes in substance should be made, noting that those relating to covenants running with the land were the subject of consideration by PLERC when, on its recommendation, section 64A was added to the statute in 1986 (see PLERC's *Report on Positive Covenants Affecting Land* (1985)). Sections 63 to 69 appear to require no change in substance though it may be possible to state some of them more concisely.

260 Section 70 is concerned with the construction of covenants and could well be combined with section 13, which provides for the construction of the word "month". Section 13 applies only to deeds, wills, orders and instruments executed or made after 5 December 1944 (the date of the passing of the Law Reform Act 1944). Now that almost 50 years have gone by the Commission questions whether there is likely to be any injustice in making the section of general application. It seems unlikely that any calculations in relation to property are today ever made on the basis of lunar months. We suspect that in practice that was hardly ever done since well before the change to the law in 1944. We are, however, concerned to know whether our view is correct and whether there may be isolated examples where lunar months are still used relying on the ancient law.

261 Part VI of the Act (sections 72 to 75) sets out a series of covenants to be implied in conveyances and leases. Covenants relating to mortgages are found in section 78 which is in Part VII. In all cases the covenants are optional in the sense that they apply only when the parties do not expressly or impliedly exclude them. They do not stand against an express exclusion and may be impliedly excluded when contradicted by the terms of a conveyance. We do not suggest that this position be changed.

262 However, sections 72 (covenants implied in conveyance by way of sale) and 73 (covenants implied in conveyance subject to encumbrance) do not apply to Land Transfer land. This means that in practice they are obsolete. A conveyance of land transfer land has *no* covenants implied into it unless it is in registrable form and, in that case, until actually registered. After registration covenants for further assurance are implied by section 154 of the Land Transfer Act. Although there seem to have been few, if any, practical problems caused by the absence of implied covenants in relation to conveyances of unregistered interests in land transfer land, the Law Commission believes that persons taking such an interest should have the benefit of general implied covenants, broadly along the lines of those now applicable to deeds system land, and therefore proposes that a set of

implied covenants be included in the new Act. They would have to be consistent with the Land Transfer Act but, in view of the intention that the Property Law Act should generally continue to be read subject to the Land Transfer Act, we do not anticipate any difficulty on that account.

263 In outline, the implied covenants which we suggest would be as follows:

(a) In transfers or assignments of land:

- warranty of right and power to transfer clear of encumbrances save as mentioned in the transfer or assignment document;
- covenant for quiet enjoyment in limited form (ie, against disturbance by the transferor and persons claiming through the transferor); and
- covenant for further assurance.

(b) In transfers or assignments of land subject to an encumbrance, a covenant by the transferee or assignee to pay moneys and perform obligations secured by the encumbrance and to indemnify in respect of them. The personal liability of executors, administrators or trustees would be excluded where notice of the capacity in which the transferee or assignee was acting had been given before the contractual relationship was entered into. Compare section 96 of the Land Transfer Act.

(c) In transfers or assignments of leases of land, a covenant by the transferor or assignor that the rent has been paid and covenants and conditions performed and observed up to the date of transfer or assignment.

(d) In such transfers or assignments by trustees and other persons mentioned in the present section 75, these covenants would not apply and would be replaced by covenants that a transferor or assignor has not and will not

- invalidate the transfer or assignment;
- cause the interest of the transferee or assignee to be defeated or the title encumbered; or
- prevent the transfer or assignment.

(e) In encumbrances (including mortgages and charges), covenants that the encumbrancer has the necessary right and power to encumber the property free and clear of encumbrances save as

disclosed and for further assurance (better encumbrancing). This implied covenant would relate to personal property as well as land and in this context would apply to a transfer or assignment of personal property by way of mortgage (ie, a legal mortgage).

264 In the Fourth Schedule to the Property Law Act there is set out a series of covenants implied by mortgagors of land. The Commission believes that it will be useful to have in the new Act a fresh set of such implied covenants and a corresponding set for mortgages over goods. (At para 336 we discuss the manner in which "goods" could be defined.) Implied covenants in relation to chattels are now to be found in the Fourth Schedule to the Chattels Transfer Act 1924 but that is a statute primarily concerned with registration of charges and, in any event, will be repealed if and when the Personal Property Securities Act is enacted as recommended by the Law Commission in its Report No 8: *A Personal Property Securities Act for New Zealand* (1989).

265 The Commission has not yet proceeded beyond preliminary work on the format of implied covenants for mortgages but has in mind, in the case of land mortgages, adapting such portions of a commonly used form as may be appropriate to every mortgage. Specialised provisions are obviously beyond the scope of a set of provisions which are to apply if the parties fail to express themselves. We consider that if suitable modern forms of covenant are incorporated in schedules to the new Act, conveyancers may feel able to incorporate them in their mortgage documentation by reference and thereby to shorten their documents. It may also be possible to use these provisions when it becomes possible to register master documents under the Land Transfer Act as is done in certain of the Australian states. (By "master documents" we mean forms of mortgages which are registered under the Act and given a registration number, and the terms of which are then incorporated by reference in a large number of other documents.)

Questions:

Q51 Is there any need to make amendments of substance in any of sections 63 to 69?

Q52 Can sections 13 and 70 be amalgamated, dropping out the reference to the Law Reform Act 1944 in the former?

Q53 Should there be implied covenants, along the lines described in para 263, in conveyances and mortgages?

PART C: MORTGAGES

IX
MORTGAGES OF LAND

FORMS OF MORTGAGES OF LAND

266 Under the general law, mortgages of land can take several forms which are very broadly summarised as follows.

- The legal mortgage, in which title is transferred to the mortgagee subject to an equity of redemption in the mortgagor.

- The mortgage by way of demise, involving a lease of the land by the mortgagor to the mortgagee (subject to a proviso that the lease term will end on repayment) followed by the mortgagor attorning (sub)tenant to the mortgagee. This gives the mortgagee the ability, upon default, to distrain on the mortgaged premises. (Compare section 107 of the Land Transfer Act conferring on a registered mortgagee a right to distrain on goods of the occupier or tenant of the property. This section would be repealed if distraint were to be abolished, as is proposed in para 569.) This device is never, so far as we are aware, used in New Zealand.

- The mortgage of a lease by way of subdemise, in which the mortgagee becomes a sublessee and avoids privity of estate with the head lessor. This carries with it the risk of forfeiture of the head lease and appears to be relatively uncommon in New Zealand.

- The equitable mortgage (of a legal or an equitable interest), which is treated, once money has been advanced, as a contract to execute a formal mortgage. In New Zealand equitable mortgages by deposit of title deeds have already been forbidden (section 77 of the Property Law Act).

- The equitable charge, a right of recourse to the property, which is appropriated to meet the debt. This is in common use in New Zealand, a typical example being a company debenture.

267 The Land Transfer Act created a statutory form of mortgage which is unknown to the general law: *a legal mortgage by way of charge*. It is a mortgage which has effect at law and not merely in equity but is in a form which, under the general law, would have been entirely equitable in character. Section 100 of that Act states that a registered mortgage shall have effect as security "but shall not operate as a transfer of the estate or interest charged". Section 101 then prescribes a set of mortgage forms which are found in the Second Schedule to the Act and are by way of charge. In

England the Law of Property Act 1925 also created a species of legal mortgage by way of charge. It has in practice "almost entirely superseded the mortgage by demise" (Law Commission of England and Wales, Working Paper No 99, *Land Mortgages* (1986) para 2.3).

268 In New Zealand it remains possible for *unregistered* mortgages of land - where the interest being mortgaged is unregistered or it is not intended to register the mortgage - to take the various forms available under the general law. As an example, it is not uncommon to find a mortgage of an unregistered lease drawn in the form of an assignment to the mortgagee but subject to a right of redemption, which is often signified by the use of the words "by way of mortgage only", qualifying the assignment.

UNREGISTERED MORTGAGES OF LAND - PROPOSALS FOR REFORM

269 We make two proposals in relation to the powers of equitable mortgagees and chargees. First, we suggest that all equitable mortgagees and chargees should be given the same powers of sale and entry into possession as a mortgagee who is registered under the Land Transfer Act (a legal chargee) and that the proposed new Property Law Act should give the court express power to provide assistance in the realisation of the power of sale.

270 Secondly, we propose that all mortgages of land should operate as charges, thus abolishing the legal mortgage, the mortgage by way of demise, the mortgage of lease by subdemise and the equitable mortgage. The only remaining forms of mortgage of land would be the registered Land Transfer mortgage (a legal charge) and the equitable charge.

271 While the first of these reforms could be effected separately, the Law Commission thinks that it leads logically to the second which is consistent with, and indeed assists, the proposals which we will make later in this paper for reform of the law relating to the running of covenants in a lease (paras 421 to 424).

272 In England, doubt has been expressed whether a mortgagee under an equitable mortgage can enter into possession, since it is said that he or she has neither a legal estate in the property nor the benefit of a contract to create one (*Ladup Ltd* v *Williams & Glyn's Bank plc* [1985] 1 WLR 851, 855). There is doubt also whether an equitable mortgagee can exercise power of sale of the legal estate, at least in the absence of an appropriate power of attorney from the mortgagor (see Fisher & Lightwood at 402-403). In England, some assistance is given to an equitable mortgagee by section 90 of the Law of Property Act 1925. Under that section the court is authorised, in making an order for sale under an equitable mortgage of land, to vest the property in a purchaser or appoint someone to convey the land or create and vest in the mortgagee a legal term of years absolute to enable the mortgagee to carry out the sale, as the case may require.

273 In New Zealand the inclusion of a charge in the definition of a mortgage in section 2 of the Property Law Act already has the consequence that, by virtue of section 78, a chargee has the power of sale implied into "mortgages of land" by the Fourth Schedule to the Act even if the charge itself gives no such express power. (See, however, *DFC Financial Services Ltd* v *Samuel* [1990] 3 NZLR 156, 167 - discussed at para 292 of this paper - in which it was said that "mortgage of land" does not include a company debenture.)

274 The Fourth Schedule makes no mention of entry into possession. There is therefore in New Zealand the same doubt as in England about the ability of an unregistered (and, therefore, equitable) mortgagee to enter into possession in the event of default by the mortgagor. For the position in Australia and New Zealand, see C E Croft *The Mortgagee's Power of Sale*, paras [60]-[68] arguing, however, that no express term is required.

275 An unregistered mortgagee certainly cannot execute a memorandum of transfer of the mortgagor's registered interest in the land in the absence of a power of attorney to do so; but the court may have an inherent power to authorise the Registrar to execute a transfer on behalf of the mortgagor, as it does to enforce a specific performance decree. This point seems never to have been determined. If the court has no such power the equitable mortgagee may have to procure registration of the mortgage before proceeding to exercise power of sale and may experience great difficulty or delay in so doing. There may be an implied obligation on the mortgagor to do all that is necessary to vest a legal charge (registered Land Transfer mortgage) in the mortgagee but, if so, it is often likely to be hard to enforce. It seems to the Commission that the court should be able to give help. However, the court, in affording equitable assistance, should retain its power to impose such conditions as it thinks appropriate, including delaying the sale where an immediate sale may be harmful to the mortgagor (see *Sheath* v *Hume* (1903) 23 NZLR 221).

276 The Commission suggests that in a new section it might be expressly provided that the holder of an equitable mortgage or charge might, upon default and subject to giving any prescribed warning notice, in exercise of power of sale (express or implied), sell the mortgagor's legal estate in the property or enter possession of the estate unless the mortgage or charge restricts that action.

277 Conferment of an express power of sale and a power to enter into possession by statute on equitable mortgagees and chargees would not, it is thought, discourage them from seeking the protection of registration any more than is now the case. We emphasise that our proposal would be subject to anything to the contrary in the bargain between the mortgagor and the mortgagee and would not alter priorities between securities given by the mortgagor. As we have pointed out, the power of sale already exists in the case of an unregistered mortgage or charge (other than a debenture), though the means of giving effect to it may currently prove

defective. The other power - to enter into possession - is often conferred by the mortgage documents. The effectiveness of such a clause in an unregistered mortgage has yet to be determined, but we are not aware of any practical objection to it. If the mortgagor does not wish to confer power of entry into possession on an equitable mortgagee, the mortgage document can make this clear.

278 The Commission envisages that a further new section could empower the court, on the application of an equitable mortgagee or chargee and upon being satisfied that the mortgagor was in default, to:

- make an order for sale (either privately or through the Registrar);
- appoint the Registrar to execute any document necessary to give effect to a sale;
- make orders concerning the conduct of the sale (including an order permitting the mortgagee to become the purchaser);
- make an order determining the priorities of securities over the mortgaged asset; and
- make an order vesting the property in any purchaser (where the sale had already occurred).

279 Although we have discussed this question with particular reference to mortgages of land, the Law Commission sees no reason why the proposed new section concerning the assistance of the court should not apply to mortgages generally.

280 If the theoretical possibility of creating a legal mortgage over an unregistered short-term lease (ie, one year or less, if our suggested reform on this point is adopted: para 91), which is itself a legal lease without registration, is put to one side, then it can be said that all mortgages of unregistered interests in land and all unregistered mortgages of registered interests in land are in New Zealand merely equitable interests. In short, all unregistered mortgages of land are equitable interests.

281 We have proposed that a holder of a charge should along with an equitable mortgagee have essentially the same powers as a mortgagee holding a legal interest. If a chargee is given all the necessary powers of enforcement of the security, there would seem to be little point in taking security other than by way of charge. To purport to assign the mortgagor's fee simple interest in land by way of mortgage (ie, using the form of a legal mortgage) would, if it were ever done, result in nothing more than an equitable mortgage. It would not be in registrable form. In the case of a leasehold interest the use of a mortgage in legal form may have adverse consequences for the mortgagee, particularly if the mortgagee goes into possession. The mortgagee might be held to be an assignee of

the lease regardless of whether the lessor has given consent (*Old Grovebury Manor Farm Ltd v W Seymour Plant Sales & Hire Ltd* (No 2) [1979] 1 WLR 1397) and, accordingly, by virtue of privity of estate, be liable for payment of rent and observance of tenant's covenants under the lease. It is presently uncertain whether a mortgagee who takes an equitable assignment of a lease or a legal assignment of an equitable lease and does not go into possession is in privity of estate with the head lessor (*Purchase v Lichfield Brewery Co* [1915] 1 KB 184; *De Luxe Confectionery Ltd v Waddington* [1958] NZLR 272 and R T Fenton, *Assignments of Informal Leases* (1977) 7 NZULR 342). Despite the uncertainty of the present position, mortgagees of unregistered leases often risk taking assignments by way of mortgage, apparently because a security in the form of a charge may present problems when enforcement is necessary. This reinforces us in our view that we should recommend extension of the powers and rights of chargees. Furthermore, our proposals on the running of the burden of lessee's covenants upon assignment of the lease (para 415) would make assignees of equitable interests directly liable to lessors before possession was taken. Therefore, a mortgagee holding under a document in the form of an assignment of a lease would become directly liable to the lessor for performance of the mortgagor/lessor's covenants. But if a chargee is given the same powers as a mortgagee it will not be necessary for someone taking security over a lease to incur this liability: the security can be taken as a charge.

282 But we would suggest a further step. Once chargees have all necessary powers conferred upon them by the statute the whole position can be simplified and unnecessary forms of mortgage eliminated by providing that, in the case of land, every mortgage or charge, no matter what its form, shall be construed as a charge unless it takes the form of a registered memorandum of transfer (as is often done in the case of submortgages). In England sections 85 and 86 of the Law of Property Act 1925 already provide that mortgages of estates in fee simple or fixed term leases are only capable of being effected in law either by a demise (or subdemise) for a term of years absolute or by a charge by deed expressed to be by way of legal mortgage. The Commission sees no need to preserve in New Zealand the highly artificial mortgage by way of demise nor does it see need for continued use of the mortgage of lease by demise if adequate assistance is given by the statute to all chargees who wish to exercise power of sale or to enter into possession. We note also that the Law Commission in England and Wales has suggested in its Working Paper No 99 on *Land Mortgages* (1986) para 6.3 that equitable mortgages by assignment should be abolished and that the only method of mortgaging or charging an equitable interest should be by way of equitable charge. Such a reform would in New Zealand be entirely consistent with the land transfer system.

283 If the law were reformed in the manner just discussed it would be unnecessary to carry forward into a new Act any equivalent of section 88 of the Property Law Act. It provides that a mortgagor who is entitled to possession or receipt of the rents and profits of any land, if no notice has

been given by the mortgagee of intention to take possession or receive rents and profits, may sue for possession or the recovery of rents or profits or damages for trespass. In the case of a security which takes effect as a charge only, there is no need for any such statement, the mortgagor remaining the owner of the fee simple or leasehold in question and being able, subject to the terms of the security, to deal freely with the property. Leases, easements and other interests in the property created by the mortgagor after the giving of the mortgage are not binding on the mortgagee unless consent is given. Pending entry into possession by the mortgagee, the mortgagor has the right to occupy the property and receive the rents and profits and to protect his or her interest by bringing claims for trespass and doing such other things as are necessary for the protection of the property. The Commission would be interested to know whether it is thought that there is any need for these things to be stated in the new Act.

Questions:

Q54 **Should equitable mortgagees and chargees of real and personal property be given implied powers to enter into possession or sell the mortgaged property (including the mortgagor's legal estate therein) in the event of default by the mortgagor - but subject to any express provision in the mortgage to the contrary?**

Q55 **Should the court be empowered on the application of an equitable mortgagee or chargee to make the orders described in para 278?**

Q56 **Should these powers be extended to equitable mortgagees and chargees of personalty?**

Q57 **Should mortgages of land in New Zealand always operate by way of charge only?**

Q58 **If so, is there any need for a section in the new Act equivalent to section 88?**

POWERS OF MORTGAGEE OF LAND

284 The Property Law Act contains no general statement concerning the powers of a mortgagee (other than the optional implied powers in the Fourth Schedule) but proceeds to impose restrictions on the way in which powers may be exercised (section 92). This position may be contrasted with registered mortgages: section 106 of the Land Transfer Act makes a positive statement that a mortgagee, upon default, may enter into possession by receiving rents and profits or may bring an action for possession of the land either before or after any sale of the land is effected under the power of sale given or implied in the mortgage. Section 106 empowers a registered mortgagee to enter into possession without first bringing an

action for possession provided the entry is peaceable (*Lysnar v National Bank of NZ Ltd (No 2)* [1936] NZLR 541).

285 The Commission considers that the clarity of the law relating to mortgages would be improved if, in the case of mortgages of both land and personal property, the new Property Law Act contained direct statements setting out the general powers of the mortgagee (subject to anything to the contrary in the mortgage document) in the event of default. In the case of mortgages of land (both registered and unregistered) such a statement could provide that upon any default by the mortgagor the mortgagee might, subject to giving the prescribed notice of the kind now required by section 92 and to any express term of the mortgage:

- enter into possession peacefully (ie, without committing forcible entry in terms of section 91 of the Crimes Act 1961) by physically taking possession; or
- enter into possession by requiring a tenant or occupier to make payment to the mortgagee of the rents and profits of the property; or
- bring proceedings seeking an order for possession.

Any of these things might be done before or after the exercise of the power of sale. (Our proposal concerning personal property is at para 337.)

RESTRICTION ON EXERCISE OF MORTGAGEE'S POWERS IN RELATION TO LAND

Notice to defaulting mortgagor

286 The concept of requiring a mortgagee of land to give the mortgagor one month's notice before exercising power of sale, entry into possession, or calling up moneys under an acceleration clause is well accepted. The idea is to give the mortgagor a final opportunity to put right defaults and thereby avoid the harsh consequences of enforcement action. It amounts to a moratorium for a short period.

287 Section 92 is expressed in a dense manner which makes for difficulty in quick understanding. We set out in para 300 a draft of three new sections restating section 92, with some changes in substance.

288 Section 92(1) requires a notice complying with section 92(2) to be given to the owner for the time being of any land before a power to sell the land or to enter into possession is exercised or before an acceleration clause is invoked in respect of any money secured by any mortgage over that land. An acceleration clause is one under which, despite the term of the mortgage being fixed by agreement, the mortgagee can by reason of default call up the mortgage moneys, or the moneys automatically fall due, if default occurs: it is to be distinguished from a right to call up moneys "upon demand"

regardless of default, where the basis of the contract is that payment can be required at any time. The person who must be given the notice is the "owner" of the mortgaged land, ie, the original mortgagor or, where the land has changed hands since the mortgage was given, the present registered proprietor (section 92(10)). In *Commodore Pty Ltd* v *Perpetual Trustees Estate & Agency Co of NZ Ltd* [1984] 1 NZLR 324 it was held that section 92(1) required notice to be given and expire before the use of an acceleration clause in claims against persons other than the mortgagor - in particular, against guarantors. In *Commodore* the borrower had given a mortgage. In *BNZ Finance Ltd* v *Smith*, a decision of the Court of Appeal on 14 June 1991 (CA 230/90), it was held that it made no difference that the borrower had not given a mortgage, the mortgage securities having there been given only by co-guarantors of the respondents to the appeal. Section 92 notices to those co-guarantors had not expired when the mortgagee first (invalidly, as it was held) made demand on the respondents under an acceleration clause. So, whenever an acceleration clause is being used in respect of moneys secured by a mortgage given by *any* party to the borrowing transaction in any capacity, it is first necessary that a notice under section 92(2) has been given *to every mortgagor* and has already expired. (It should be observed, nevertheless, that in *BNZ Finance Ltd* v *Smith*, Richardson J thought that section 92(1) did not apply to a claim under an unsecured guarantee against a guarantor who was not a principal debtor.) However, it was also found in *Commodore* that, once a power of sale has been validly exercised, so that moneys to which an acceleration clause relates are no longer secured by a mortgage of land, the restriction on the subsequent use of an acceleration clause ceases. We intend in our draft sections to preserve all of these rules.

Notice to covenantors

289 Section 92(6) provides that, if at any time the mortgagee exercises the power of sale conferred by a "mortgage of land", no action to recover a deficiency is to be commenced by the mortgagee against any person other than the owner of the land at the time of exercise of the power of sale, unless the mortgagee has at least one month before exercise of the power of sale served on that person notice of intention to exercise the power of sale and to commence action against that person to recover the deficiency in the event of the amount realised being less than the amount owing under the covenant to repay.

290 Section 92(6) is draconian: it may entirely release a covenanting party (guarantor or original mortgagor) to whom notice has not been given of the intent to exercise power of sale and claim any deficiency. The guarantor is released regardless of whether there has been prejudice caused by the absence of timely notice. However, a strange consequence of the present wording of the subsection is that it may not apply where proceedings are issued against the guarantors or the original mortgagor *before* a mortgagee sale takes place (see

the judgments of Somers J in *Commodore*, of Somers and Hardie Boys JJ in *DFC Financial Services Ltd* v *Samuel* [1990] 3 NZLR 156 and Casey J in *BNZ Finance Ltd* v *Smith*. But the contrary view is expressed in the judgments of Cooke and Bisson JJ in *Commodore*, Bisson J in *Samuel* and Cooke P in *BNZ* v *Smith*). This issue does not seem to have been finally resolved.

291 The Law Commission believes that a mortgagee who is proposing to exercise power of sale conferred by a mortgage of land (including a debenture) should be required at least 20 working days before exercising that power to serve upon a covenantor a notice stating that intention and advising that any deficiency after sale will be claimed from that person. By "covenantor" we mean a person (other than the registered proprietor at the time of sale) who has agreed to pay or is otherwise liable to pay any part of the moneys secured by the mortgage. However, failure to comply with this requirement should not prevent exercise of the power of sale and should not release a covenantor except to the extent that the covenantor can show prejudice arising from the failure. To the extent that prejudice is demonstrated by the covenantor, there would be a release from liability to the mortgagee in respect of the deficiency. It would not be possible to contract out of this stipulation. The new section should be so worded that it applies whenever the amount sought to be recovered constitutes a deficiency, ie, an amount by which the moneys available to the mortgagee after the exercise of power of sale are less than the amount owing to the mortgagee and secured by the mortgage at the time of the sale.

Receivers

292 The relationship between section 348(8) of the Companies Act 1955 and section 92 has caused difficulties. Although a mortgagee must give notice before entering into possession of land or calling up the moneys owing pursuant to an acceleration clause, section 92(1) does not prohibit an action of that kind by a receiver who is acting as the agent of a mortgagor company. Indeed, section 92(1) is said to draw a distinction between a "mortgage", which includes a debenture, and a "mortgage of land", which does not (see the judgments of Hardie Boys J in *DFC Financial Services Ltd* v *Samuel* at 167 and Somers J at 162). Sale and entry into possession are forbidden in respect of any "mortgage"; acceleration is forbidden only in respect of a "mortgage of land", so it is permissible under a debenture. This is consistent with section 348(8) which says that nothing in section 92 requires the giving of a notice under that section before "any money secured by the debenture becomes payable".

293 The Law Commission thinks that a debenture holder should remain exempt from the obligation to give a notice under section 92 before appointing a receiver, who takes possession, or before calling up the moneys secured by the debenture, but that, as at present, power of sale should not be exercisable under the debenture either by the debenture holder or the receiver before expiry of a notice under section 92. But when referring to a debenture we do not intend to

include an ordinary mortgage of land, nor should the exemption apply if there is a collateral mortgage of land. The existence of a collateral mortgage of land will in most instances indicate the importance of the land as a security. It should not be possible to avoid the requirement for a notice by using the powers of entry into possession and acceleration under the debenture. We recognise that in some instances the mortgage may be of lesser importance than the debenture but can see no way to identify such instances in legislation. As the notice is for a short period only (20 working days) and must be given in all cases before any sale, we think that in the substantial majority of cases there is unlikely to be prejudice to a debenture holder who is prevented, because of the existence of a collateral mortgage, for that short time from calling up the amount outstanding or from entering into possession. If the mortgagee is prejudiced, a dispensation can be sought from the court - and this can be done ex parte if there is good reason not to alert the debtor before putting in a receiver.

294 Since the Law Commission published its report on company law (Report No 9) the Court of Appeal has found in *DFC* v *Samuel* that section 92(6) does not require a receiver to give a notice to a covenanting party warning of the likely claim for a deficiency after exercise of a power of sale. The Law Commission thinks that there is good reason for a guarantor in some circumstances to be released from liability, or have that liability reduced, if the receiver fails to tell the guarantor of a pending sale and prejudice is shown resulting from this omission. There should be no distinction in this respect between a sale by a mortgagee and a sale by a receiver. Somers and Hardie Boys JJ in *DFC* v *Samuel* found that there is such a distinction in the present law. Our scheme of section 92 would change this position.

Form of notice

295 One difficulty which often faces a mortgagee giving a notice under section 92(1) is that the mortgagee cannot be sure when the notice will be served. The amendments made a few years ago to section 152, dealing with service of notices, have added to this risk. If, unbeknown to the mortgagee, there has been a delay in service of the notice, the time between service and the date which has to be stipulated in the notice (see *Sharp* v *Amen* [1965] NZLR 760) may be less than the prescribed period of notice. Although it does not entirely solve the problem from the point of view of the mortgagee, the position of that party may be enhanced without undermining the rights of the mortgagor if the notice takes the form of advice to the mortgagor that the period in question is, say, 20 working days from the date of service of the notice. Under our proposals for a new notice section (para 658) - abolishing the deemed service in ordinary course of post - it should be readily apparent to the mortgagor when the notice has been validly served.

296 Where there is more than one person to be served as mortgagor, the notice should run from the date on which the

last of those persons is served. Each would know that he or she had at least 20 working days from the date of notice in which to comply with it. If another mortgagor was served on a later date that would amount to a "bonus" for the mortgagor who was served first. The purpose of the section - to give at least 20 working days' notice - would be achieved.

297 Every notice would have to contain the statutory definition of "working days" so the mortgagor was informed as to the meaning of that term. This definition could be in terms of the Commission's proposals for a new Interpretation Act (Report No 17 (1990)).

298 Under our proposals a mortgagee could, in the notice, demand payment of a stated sum for reasonable costs and expenses of preparing and serving the notice. The default complained of could not be cured unless this sum were duly paid.

"Stale" notices

299 It has been suggested to the Commission that a notice under section 92 should become "stale" after 12 months, so that, if the mortgagee wishes to enter into a contract of sale after that time, a fresh notice would have to be given. We are inclined to agree with this suggestion.

Draft sections

300 The draft of the proposed sections follows:

[92] Notice to registered proprietor

(1) Except as otherwise provided in subsection (6), no moneys secured by a mortgage of land are payable by any person under an acceleration clause, and no mortgagee or receiver may exercise, by reason of any default, any power to enter into possession of, or to sell, that land unless

(a) the mortgagee or receiver has, within the 12 months immediately preceding the date on which the payment of those moneys is required to be made or that power is exercised, served a notice complying with subsection (2) on the person who is the registered proprietor of the land at the date of the service of the notice; and

(b) the default has not been remedied before the expiration of the period specified in the notice.

(2) The notice required by subsection (1) must be in the form prescribed by regulations made under this Act, or in a form to like effect, and must adequately inform the registered proprietor of

(a) the nature and extent of the default complained of; and

(b) the action required to remedy the default (if it is capable of being remedied); and

(c) the period within which the registered proprietor must remedy the default or cause it to be remedied, being not less than 20 working days after the date of service of the notice, or any longer period for the remedying of that default specified by any term expressed or implied in any contract; and

(d) the consequence that if, at the expiration of the period specified under paragraph (c), the default has not been remedied, the specified moneys secured by the mortgage will become payable, or may be called up as becoming payable, or the specified powers will become exercisable, or any of those things as the case requires.

(3) The notice given under this section may specify that the action required to remedy the default complained of includes the payment to the mortgagee of a specified amount, being the mortgagee's reasonable costs and disbursements in preparing and serving the notice.

(4) A notice under this section may be given in the same document as a notice under section 90 [Mortgagee accepting interest not to call up without notice].

(5) A mortgagee or a receiver serving a notice on a registered proprietor in accordance with this section must, as soon as possible, serve a copy of the notice on:

(a) any mortgagee or encumbrancer of the land whose mortgage or encumbrance ranks in priority after the mortgagee's mortgage and of whose name and address the mortgagee or receiver has actual notice; and

(b) any person who has lodged, under the Land Transfer Act 1952, a caveat or a matrimonial property notice against the title to the mortgaged land or any part of it;

but a failure to comply with this subsection does not of itself prevent any moneys secured by the mortgage from becoming payable or prevent the mortgagee or receiver from exercising any power to enter into possession of, or to sell, the land.

(6) Where a mortgage of land arises only under a debenture, and there is no collateral mortgage of land securing the same moneys

(a) a receiver may exercise any power to enter into possession of the land conferred by any term expressed or implied in the debenture; and

(b) moneys secured by the debenture may become payable under an acceleration clause;

without notice being given under this section.

(7) Any term expressed or implied in any instrument and conflicting with this section is of no effect.

(8) For the purposes of this section

acceleration clause means any term expressed or implied in any contract under which, by reason of any default, any moneys secured by a mortgage of land become payable, or may be called up as becoming payable, on a date earlier than that on which they would have become payable had the default not occurred;

debenture means an instrument creating a charge on both land and other property, that property being all, or substantially all, the assets of the chargor;

default means any default in the payment on the due date of any money payable under any instrument or any failure to perform or observe any other term expressed or implied in that instrument;

mortgage includes a mortgage of land and **mortgagor** and **mortgagee** have a corresponding meaning;

mortgage of land includes a mortgage of land arising under a debenture;

registered proprietor means the person named in any grant, certificate of title or other instrument registered under the Land Transfer Act 1952 as seised of or taking any estate or interest in land, and includes any person otherwise seised or possessed of any estate or interest in land, at law or in equity, in possession or expectancy;

working day means ... [as in s19 of the draft Interpretation Act in the Law Commission's Report No 17: *A New Interpretation Act*].

[92A] Notice to covenantor

(1) A mortgagee or a receiver who, by reason of any default, is proposing to exercise any power to sell any land and to recover any deficiency on that sale from any covenantor, must serve notice of those intentions upon that covenantor at least 20 working days before exercising the power of sale.

(2) Failure to serve notice under subsection (1) on any covenantor shall not prevent the mortgagee or the receiver from exercising the power of sale, or recovering any deficiency from that covenantor, but a covenantor who can show that he or she was prejudiced by that failure is, to the extent of that prejudice, released from liability to the mortgagee or receiver in respect of the deficiency.

(3) Any term expressed or implied in any contract and conflicting with this section is of no effect.

(4) For the purposes of this section

covenantor means a person (other than the registered proprietor of the mortgaged land at the time of the sale) who has agreed or is otherwise liable to pay the moneys secured by the mortgage or any part of them;

default means any default in the payment on the due date of any money payable under any instrument or any failure to perform or observe any other term expressed or implied in that instrument;

deficiency, in relation to any sale, means any amount by which the amount received on that sale and available to a mortgagee in accordance with [section 104 of the Land Transfer Act 1952 - to be transferred to the Property Law Act] is less than the amount owing to the mortgagee and secured by the mortgage.

[92B] Court may give leave to enter into possession

A court may, upon such terms and conditions (if any) as it thinks fit, grant leave to a mortgagee [or a receiver] of any land (upon an application made ex parte or otherwise as the court thinks fit) to exercise any power to enter into possession of that land, by reason of a default under the mortgage,

(a) without serving the notice required by section 92(1); or

(b) after serving that notice but before the expiration of the period specified in that notice for the remedying of the default.

301 In considering the draft sections it should be noted that:

(a) The intention is to provide a moratorium (pending expiry of the notice) on the use of an acceleration clause and the exercise of the powers of sale and entry into possession where

- the mortgage has been given by the current registered proprietor to secure that person's debt;
- the mortgage has been given by a former registered proprietor to secure that person's debt; or
- the mortgage has been given by a guarantor against whom enforcement action is being taken.

(b) If a guarantor has given a mortgage but is not a principal debtor the section will require notice to that guarantor before entry into possession or sale but not before exercise of an acceleration clause in the principal loan contract. However, if that guarantor is a principal debtor (as is usually the case) the liability will be under the principal loan contract and notice to him or her will be required before use of the acceleration clause therein.

(c) A receiver may be appointed to act as the agent of the debtor under a general debenture or under a mortgage.

(d) The section does not prevent appointment of a receiver but does delay until expiry of a notice the taking of possession by a receiver, unless the entry is pursuant to a general debenture and there is no collateral security by way of mortgage.

(e) No receiver, whether under mortgage or debenture, may exercise a power of sale of land without notice having been given and expired.

(f) If in a particular case there is urgent need for a receiver to take possession under a mortgage, or under a debenture where there is a collateral mortgage, an application can be made to the court under section [92B]. A mortgagee or debenture holder can also apply under this section.

Question:

Q59 Should section 92 be restated along the lines of the provision set out above?

MORTGAGEE IN POSSESSION OF LAND

302 Only two sections of the Property Law Act - sections 91 and 95 - deal with the position of a mortgagee in possession. Section 91 is the more important and is concerned with the powers of the mortgagee in connection with the leasing of the property. Section 95 gives power to cut and sell trees. The Commission has formed the provisional view that further matters should be dealt with by the proposed new Act so that, although it would not contain a code relating to mortgagees in possession, some of the existing law would be stated and clarified and some unsatisfactory elements of the law, including section 91, could be modified.

Leasing powers

303 Section 91 requires that a mortgagee in possession must not grant a lease for a term exceeding seven years. A lease purported to be granted by the mortgagee for a term longer than seven years takes effect against the mortgagee by estoppel only and is not binding on the mortgagor (*Smith* v *Jordan* [1953] NZLR 160). A term of that length seems too long in the case of a residential tenancy and too short for a commercial lease. The Commission suggests that two years is an adequate maximum period for a residential tenancy while 15 years, which is in line with modern commercial leasing practice of a kind likely to attract the best terms and conditions for the lessor, would be a suitable maximum for other properties. But is it too long for a farm or horticultural property?

304 A new Property Law Act could also usefully:

- contain a requirement that a mortgagee in possession should, in granting a lease, have reasonable regard for the interests of the mortgagor;
- require that, when leasing, a mortgagee in possession should take all reasonable care to obtain the best rent reasonably obtainable as at the time of the leasing;
- provide that, except with the consent of the mortgagor or the court, any such lease should contain (and contain only) terms and conditions ordinarily found in leases of comparable properties in the district; and
- provide that, when the mortgagee ceases to have possession, the benefit and burden of the covenants run with the reversion in favour of and

against the mortgagor or anyone to whom the property is transferred (subject to the Land Transfer Act).

305 Section 91(11) already provides that a mortgagee in possession of land is entitled to sue upon the covenants of existing leases affecting the land and to exercise the rights, powers and remedies of the lessor under the lease in all respects as though the reversion were vested in the mortgagee. It does not matter whether the lease has been granted by the mortgagee or the mortgagor or any other person. The Commission proposes that a provision along these lines should be brought forward into the proposed new Act. It could be made clear that the mortgagee may bring proceedings in respect of breaches occurring prior to the taking of possession, including a claim for rental which fell due for payment before the entry into possession.

Application of moneys

306 Moneys received by a mortgagee in possession have to be applied in the following order:

- payment of outgoings on the property (including payments made in respect of any mortgage having priority);
- payment of costs relating to the taking and holding of possession (for example, agent's fees for leasing and managing the property);
- payment of interest;
- repayment of any moneys advanced by the mortgagee to meet reasonable expenses (including the cost of repairs and improvements);
- re-payment of principal sum;

unless the mortgagee elects to pay the moneys over to the mortgagor (Hinde McMorland & Sim at para 8.106). The order of priority should, we think, be stated in the proposed new Act.

Accounting

307 An accounting between a mortgagee in possession and the mortgagor must in the absence of special circumstances or a stipulation in the mortgage for interest rests be made as a whole (ie, without rests). Depending upon the way matters work out, this can be unfair to either party (see *Couzens* v *Francis* [1948] NZLR 567). If at any particular date the mortgagee has collected more than is needed to meet interest then due, any surplus in hand need not be treated as a payment of part of the principal sum but may be retained without allowance of interest on it (*Union Bank of London* v *Ingram* (1880) 16 ChD 53, 56). On the other hand, unpaid interest does not compound (*Union Bank of London*). It seems to the

Commission that a new Act should state rules concerning the obligation to account on the part of the mortgagee as follows:

- An accounting between a mortgagee in possession and a mortgagor (and subsequent encumbrancers) should be on the basis of all rents and profits received from the property or which would have been received but for wilful neglect or default of the mortgagee. This would appear to represent the current law (Hinde McMorland & Sim at para 8.110).

- In any such accounting the mortgagee in possession should give credit for the value of any personal occupation by way of an allowance of an occupation rent which is fair as between the mortgagee in possession and the mortgagor in the circumstances. (As at present, a mortgagee physically entering solely in order to protect the security or as a preliminary step in the sale process would not be obliged to make such an allowance. But the mortgagee should have to demonstrate that the sale was not unnecessarily delayed.)

- In any such accounting, interest should be calculated with half-yearly rests or rests of such shorter or longer period as is provided for in the mortgage document. This would reverse the law as expounded in *Union Bank of London* v *Ingram* and *Couzens* v *Francis*. It would, in effect, require the mortgagee to apply any surplus towards the principal amount and thereby receive it in instalments, even when the mortgage was on a flat basis. We see nothing unreasonable in this requirement if the mortgagee has elected to take the rents and profits by seizing possession.

Timber

308 Section 95 gives a mortgagee in possession power to cut and sell timber and other trees on the land which are ripe for cutting and not planted or left standing for shelter or ornament. A contract for the cutting and sale must be completed within any time not exceeding 12 months from the making of the contract. By virtue of section 96 this rule does not apply to mortgages of land executed before 8 September 1939. The Commission suggests that the substance of section 95 should again appear in the proposed new Act but that there is no longer any need to restrict its application in the manner now done by section 96. There are unlikely to be existing mortgages of relevant land dating from before World War II.

Receiverships

309 The Law Commission in its report on company law, Report No 9, has recommended certain reforms relating to the law of

receiverships. They have been included in the Companies (Ancillary Provisions) Bill now before Parliament with the intention that there is to be a separate Act governing receiverships. The Commission's recommendations that certain of the rules relating to receiverships should also apply to a mortgagee in possession would, if adopted, need to appear in the Property Law Act. Those provisions would be in relation to notice of appointment, obligations of the grantor upon appointment, other duties of a receiver and the ability of the court to determine or limit the receivership.

Power to manage property and carry on business

310 The Commission would be interested to learn whether it is considered that a mortgagee in possession should be empowered by statute to manage the mortgaged property and carry on any business of the mortgagor associated with the property (as is proposed in relation to receiverships in the Bill before Parliament and in the Commission's Report No 9 *Company Law Reform and Restatement*). The concept of a mortgage of land with power in the mortgagee, upon default, to carry on the business which the mortgagor has operated on the premises is found in caselaw: a power of this kind was upheld in *Burns Philp Trustee Co Ltd* v *Ironside Investments Pty Ltd* [1984] 2 Qd R 16 and *Atkins* v *Mercantile Credits Ltd* (1986) 10 ACLR 153. The power creates no proprietary interest in assets of the business other than the mortgaged land (see generally Peter Watts, "Alternative Types of Charge Over Company Businesses And The Effect of Winding Up on Them - Recent Developments in Australia and New Zealand" (1989) 12 UNSWLJ 179).

Repairs

311 The obligation of a mortgagee in possession to carry out repairs to the mortgaged property is summarised in Fisher & Lightwood:

> The mortgagee in possession is not judged by the degree of care which a man is supposed to take of his own property. He need not rebuild ruinous premises, and will not be charged with deterioration of the property arising from ordinary decay by lapse of time. He will be allowed the cost of proper and necessary repairs, and he ought to do such repairs as can be paid for out of the balance of the rents after his interest has been paid, though he need not increase his debt by laying out large sums beyond the rents. (at 370)

312 The Commission thinks that a mortgagee in possession should not have an obligation to carry out repairs which cannot be paid for out of surplus rent (or, where the mortgagee is using the premises personally, occupation rent) after the outgoings on the property have been met, and that a rule to this effect should be included in the new statute. The priority scheme in para 306 for the application of rents will need to allow for the use of surplus moneys for proper repairs. A mortgagee in possession should be liable for voluntary waste on the same basis as a tenant (see paras 574 to 576).

Withdrawal from possession

313 A mortgagee who has gone into possession may find it very difficult to withdraw from possession and terminate ongoing liability to account for rents or profits.

> I have never heard it suggested, nor do I think it is the law, that a mortgagee is entitled to go into and out of possession whenever he likes. In my opinion when once he takes upon himself the burden which is imposed on all mortgagees who are in possession, he must continue to perform the duty, and he cannot when he pleases elect to give it up. (*In Re Prytherch* (1889) 42 ChD 590, 600, North J)

In New Zealand see *Donovan* v *Hanna* [1926] NZLR 883, 886-887. The only way in which a mortgagee can avoid continuation of possession is by the appointment of a receiver acting as the agent of the mortgagor, who is then regarded as being in possession again (*Anchor Trust Co Ltd* v *Bell* [1926] Ch 805) or by applying to the court to appoint a receiver.

314 It seems to the Commission that a mortgagee in possession should be able to withdraw from possession with the consent of the court after notice of an application has been given to the mortgagor. Once the mortgagee has withdrawn in this way, there should be no further liability to account for rents or profits accruing thereafter but, equally, no entitlement to those rents or profits or to any other moneys received by way of rents or profits whether accruing before or after withdrawal - save that where, in any accounting between the mortgagee in possession and the mortgagor, the mortgagee has been liable for rents and profits not actually received, the mortgagor should be required to reimburse the mortgagee to the extent that those amounts are later actually received by or for the benefit of the mortgagor.

315 After a mortgagee has withdrawn from possession with the consent of the court, that mortgagee should not be entitled to enter into possession again without further consent from the court. This stipulation is intended to prevent a mortgagee from avoiding problems of management of the property by temporarily withdrawing. The requirement that consent be obtained before withdrawal should ensure that the property is not simply abandoned, perhaps in the absence of the mortgagor.

Provisions of Land Transfer Act

316 There are two rather difficult sections of the Land Transfer Act, sections 108 and 110, on the subject of mortgagees in possession. To the extent that they should be preserved, they would be better placed in the Property Law Act where they could apply also to unregistered interests.

317 Section 108(1) gives a mortgagee the right against a mortgagor or other occupier, where default has been made under the mortgage, to obtain possession of the land, that is, to become a mortgagee in possession, by exercising the same

remedies as a landlord would have against a tenant when the term is expired or rent is in arrear. We have already (at para 285) suggested that there should be a statement in a new Property Law Act of a power for the mortgagee (inter alia) to take possession of the land *from the mortgagor*. We think there could also be included a provision giving the mortgagee the right to recover the land, in the event of default by the mortgagor, from an occupier other than the mortgagor. This would include a lessee; but the power should not be exercisable where the mortgagee has consented to the lease. If there has been a consent, the appropriate process would be for the mortgagee to go into possession by giving notice to the lessee to pay rent to the mortgagee. Then, once in possession, the mortgagee could exercise its rights in relation to the existing lease (see para 305, above).

318 Section 108(2) of the Land Transfer Act has been described by Edwards J in *Rakera* v *Downs* [1916] NZLR 669, 674 as "a very singular provision". It appears from *Miller* v *Moffett* (1910) 12 GLR 383 that no similar section existed at that time in other Australian states and we are not aware that that position has since changed. The section states that no right of recovery of possession by any lessor or mortgagee extends to bar the right of a mortgagee *of any lease* who is not in possession if that mortgagee pays all rent in arrear and all costs and damages sustained by the lessor or person entitled to exercise the right of recovery and performs all the covenants and agreements which on the part and on behalf of the first lessee are and ought to be performed. A mortgagee of a lease who cannot remedy a breach of covenant or condition on the part of the lessee (eg, where the lessee is bankrupt) cannot invoke the subsection. Section 108(2) is not consistent with the general discretionary scheme of section 118(2) of the Property Law Act (relief against forfeiture); it applies only to registered leases (which in itself seems anomalous) and it is not apparently subject to any overriding right of a mortgagee of the reversion who has not consented to the lease unless it is supposed to be read subject to section 119. This point is unclear. The court has no discretion and *must* stop the lessor or the mortgagee of the reversion from forfeiting the lease (*Rakera* v *Downs* at 674). To the extent that it applies to recovery by a lessor for non-payment of rent it seems unnecessary since, as we point out at para 549, the court will rarely refuse to reinstate the lease if rent arrears are paid. In any other case the discretion of the court would presumably be exercised in favour of the mortgagee of the leasehold under the relief section which we are now proposing (paras 543 to 554). Indeed, the mortgagee of the leasehold would be slightly better off because discretionary relief might well be available even where the breach of the lease could not be remedied. A mortgagee of the reversion who has not consented to the lease should not be bound at all. It would seem better that section 108(2) be repealed and that the parties to the situation which it contemplates should obtain their remedies exclusively under a new section for relief against termination.

319 Section 110 provides that a mortgagee of leasehold land or a person claiming as purchaser or otherwise from or under any such mortgage, after entry into possession of the land or

the rents and profits, shall during that possession and to the extent of any rents and profits received be liable to the lessor to the same extent as the lessee or tenant was prior to the entry into possession. Section 110 was said by Williams J in *Miller* v *Moffett* (1910) 12 GLR 383, 384 to be "not very aptly worded". He took it to mean

> that after one mortgagee of a lease has taken possession and during his possession he is liable to the lessee for breach of covenant or condition to the same extent as the original lessee was liable before the mortgagee entered, and that he takes up the position of the original lessee.

The section should be re-worded to accord with this view. It should also require payment of an occupation rent if the mortgagee benefits from personal occupation. At present it does not cover this situation (*National Mortgage and Agency Co of NZ Ltd* v *Mayor of Kaiapoi* (1888) 7 NZLR 231).

Questions:

Q60 **Are periods of leasing by a mortgagee in possession of two years for residential tenancies and 15 years for other premises suitable maximums?**

Q61 **Should it be provided that when leasing a mortgagee in possession must**

- **have reasonable regard to the interests of the mortgagor;**
- **take reasonable care to obtain the best rent reasonably obtainable at the time; and**
- **ensure that lease terms and conditions are those ordinarily found in comparable leases in the district?**

Q62 **Should the rules for application of moneys and accounting be as stated in paras 306 and 307?**

Q63 **Should a mortgagee in possession be empowered to manage the mortgaged property and carry on any business of the mortgagor associated with the property?**

Q64 **Should a mortgagee in possession be obliged to carry out repairs (other than remedying voluntary waste) where surplus rents are not available?**

Q65 **Should a mortgagee be permitted with leave of the court to withdraw from possession?**

Q66 **Should section 108(2) of the Land Transfer Act be repealed?**

POWER TO ADOPT MORTGAGOR'S AGREEMENT FOR SALE

320 Mortgagees may be assisted by provision in the proposed new Act that a mortgagee may take advantage of an agreement

for sale and purchase which has previously been entered into by the mortgagor in respect of the mortgaged land. There have apparently been situations in recent times in which an insolvent mortgagor has negotiated and signed up an agreement for sale and purchase of the mortgaged property and afterwards abandoned the property and the agreement. It is uncertain in the present state of the law whether the mortgagee has power in these circumstances to step into the shoes of the mortgagor as vendor and to enforce the agreement against the purchaser by means of specific performance or an action for damages. It could therefore be provided that a mortgagee of land who is entitled to enter into possession may enforce any agreement for sale and purchase which has been entered into by the mortgagor. The purchaser would have the same rights to defend such enforcement action as would be available against the mortgagor/vendor.

Question:

Q67 Should a mortgagee have power to adopt an agreement for sale entered into by the mortgagor?

PURCHASE OF LAND SUBJECT TO EXISTING MORTGAGE

321 Section 104 provides that where a person acquires land subject to a mortgage, unless a contrary intention appears in the document, that person becomes personally liable to the mortgagee once the land has been transferred to him or her for performance of the mortgagor's obligations under the mortgage in the same manner as the original mortgagor: it is not necessary that the transferee should have signed the transfer document. The mortgagee has a remedy directly against that person but the liability of the original mortgagor or any intermediate transferee is not extinguished. A transferee who is an executor or administrator or trustee is liable only to the extent of the trust property.

322 It has been submitted to the Commission that bankers holding under a current account mortgage cannot safely rely upon the section and must obtain a new mortgage from the transferee. Doubts have been expressed whether the words "all principal money and interest secured by the mortgage" are sufficient to cover the various kinds of banking accommodation for which security is normally afforded under a current account mortgage. The section does not cover accommodation subsequently given *to the transferor* or *any* accommodation given to the transferee. For these reasons a prudent banker will always take a fresh mortgage from the transferee. It is said that this complicates transactions between family members or related companies and it has been suggested to us that the section should be redrafted to overcome these problems. However, the Law Commission does not consider that the section should be extended in this way. It is really intended for a relatively straightforward situation, namely, one in which an advance of a specific amount has been secured against the property and the land is purchased by someone else who takes over responsibility to pay that known amount. We believe that

the section was never intended to apply to a security for a current account which continues to fluctuate after the transfer of the land. An extension of the section in this way might create more problems than it solves.

323 Indeed, it seems to the Commission that, if anything, the section should be tightened up so that it is made clear that nothing in it renders a transferee liable for any advance made to the transferor/mortgagor after notice of the transfer of the land has been given to the mortgagee except where the mortgagee was at the time of the transfer obliged to make the advance and remained obliged to make it when it was actually made. That apart, we do not propose any amendment to the substance of the section.

324 Section 104(3) states that the transferor or the transferee is not obliged to execute a covenant for the payment of the mortgage moneys and that no such covenant, contract or condition is to have any effect whatever. The Commission assumes that when section 104 was inserted into the legislation in 1952 there must have been a pre-existing practice under which deeds of covenant were executed by those requiring land subject to a mortgage and that it was intended that mortgagors be freed from the expense and trouble of continuation of this practice: the section would suffice. We would be interested to learn whether this speculation on our part is correct. If it is, we think it unlikely that the practice would now revive if subsection (3) were not brought forward into a new Act.

Questions:

Q68 **Should section 104 be restricted to liability for advances made to the mortgagor/transferor prior to the transfer coming to the attention of the mortgagee - except where the mortgagee remains obliged to make further advances?**

Q69 **Should subsection (3) of section 104 be carried forward?**

X
MORTGAGES OF PERSONAL PROPERTY

FORECLOSURE ON EQUITY OF REDEMPTION IN PERSONAL PROPERTY

325 In broad terms the mortgagee's right of foreclosure consists of an ability to obtain, by a rather cumbersome procedure, a court order extinguishing the mortgagor's equity of redemption in the mortgaged asset so that it becomes the property of the mortgagee absolutely. The mortgagee remains liable on his or her personal covenant, though the foreclosure may be reopened if steps are taken to enforce it (Sykes at 126).

326 In New Zealand, foreclosure of the equity of redemption in land was abolished as long ago as 1842, by section 41 of the Conveyancing Ordinance. The device of the Registrar's sale, a feature of which is that the mortgagee may buy in by paying the redemption price, was introduced in sections 6-10 of the Conveyancing Ordinance Amendment Act 1860 (see now sections 99 to 103 - paras 378 to 393). This is an easier route for a mortgagee to take in order to acquire the property. Strangely, however, although a Registrar's sale can in theory be conducted in respect of chattels under the Chattels Transfer Act 1924 (section 46 of which adopts sections 99-103 of the Property Law Act), foreclosure has not been abolished in respect of personalty. It seems that applications for an order of foreclosure of personalty are, in practice, never made; nor, indeed, are applications made for Registrar's sales in respect of personalty. Evidently, exercise of the ordinary power of sale of mortgaged chattels is found to be more convenient. The New Zealand experience in this respect is paralleled elsewhere: in other Commonwealth jurisdictions foreclosure is only rarely resorted to (eg, Sykes at 124; Fisher and Lightwood at 407). This seems to be because of its procedural complications, including the risk of an application for reopening.

Possible advantages of foreclosure

327 The Law Commission has been able to identify only two reasons why it might rather weakly be argued that there may be some advantage for the mortgagee in foreclosing. The first of these is where the mortgaged asset is worth less than the amount owing under the mortgage but there is a chance that the value of the asset will soon increase. However, the mortgagee does not need to foreclose in these circumstances, being able to delay exercising the power of sale until that increase occurs (*China and South Sea Bank Ltd* v *Tan Soon Gin* [1990] 1 AC 536 (PC) and *Countrywide Banking Corporation* v *Robinson* [1991] 1 NZLR 75 (CA)).

328 The other advantage relates to the operation of section 20 of the Limitation Act 1950, which expressly recognises foreclosure actions in respect of mortgaged personal property. It stipulates that a limitation period of 12 years applies "from the date on which the right to foreclose accrued". But it also provides, under certain conditions, for

what amounts to an extension of the limitation period. If the mortgagee is in possession, the right to foreclose is not deemed to have accrued until possession is discontinued. In the case of future interests or life insurance policies, the right to foreclose is not deemed to have accrued until they have matured or been determined. The Law Commission has already recommended in its Report No 6: *Limitation Defences in Civil Proceedings* (1988) para 364 that this last provision be repealed on the ground that mortgagees of future interests or unmatured life insurance policies "would be able to protect themselves by contract at the time of entry into the transaction, and that such special circumstances should not justify additional complications in a statute of limitations". In practical terms the possibility of a mortgagee remaining in possession of personal property for the length of time contemplated by the Limitation Act is remote.

329 The Commission has therefore come to the conclusion that nothing would be lost for mortgagees if the remedy of foreclosure over personal property were to be abolished.

Statutory foreclosure

330 The statutes establishing personal property securities regimes in some of the Canadian provinces provide a model for a new statutory scheme of foreclosure with the acquiescence of the mortgagor and other affected persons or by court order. The procedure is that, after default, the mortgagee can put forward to the mortgagor a proposal to accept the security in full satisfaction of the debt. If the mortgagor raises no objection within a short period (15 days) foreclosure becomes automatic. However, where the mortgagor objects, the mortgagee can apply to the court for a judicial foreclosure. If foreclosure is agreed to or ordered by the court the mortgagee is not liable to account for any surplus obtained from a future sale but, on the other hand, the mortgagor is not liable for any deficiency. The mortgagee is deemed to have irrevocably elected to retain the mortgaged asset in satisfaction of the obligation secured by the mortgage. The transaction cannot be reopened.

331 In view of the lack of use of the Registrar's sale procedure for mortgaged chattels, we anticipate that there will not be a great deal of enthusiasm for adopting in New Zealand this Canadian model. If it were considered to be appropriate, a New Zealand equivalent should, it is thought, allow a longer period for objection by the mortgagor (say, 20 working days). The form of notice to the mortgagor would need to be carefully prescribed so that there was no danger of a mortgagor misunderstanding the consequence of failing to object to a proposal by the mortgagee for foreclosure. Even then we think that automatic loss of the equity of redemption because of failure to respond to the mortgagee's notice might be most unfair. There might also be problems for the mortgagor under the income tax accruals regime to the extent that any balance of the debt was released by the foreclosure. Unless there was significant support for the Canadian model, we would think it best simply to abolish foreclosure altogether.

Questions:

Q70 Should foreclosure be abolished in respect of personal property?

Q71 Should it be replaced by the Canadian scheme described in para 330?

MORTGAGES OVER GOODS - POWERS AND RESTRICTIONS

332 The Property Law Act does not contain powers and restrictions in relation to mortgages of personal property comparable to those discussed in the preceding chapter relating to mortgages of land. One reason for the different treatment of personal property in the Property Law Act may be the belief that land is the most significant asset owned by New Zealanders. Whilst that may be so in relation to individuals it is untrue for many trading companies. Another reason for the omission may be the variety of personal property, ranging from intangibles, through negotiable instruments and other forms of paper, to goods. Moreover, even within a range of goods, there are many differences in characteristics.

333 There is also much greater variability in the types of security interests which are created over personal property (and even over goods) than for security interests over land. Personal property securities range from mortgages or charges over individual assets (most commonly in the form of an instrument by way of security) to hire purchase agreements and conditional purchase agreements, where title resides in the creditor and passes to the debtor only when the credit is paid, and financing bailments under which it may or may not be intended that the debtor should eventually acquire title to the asset. Most importantly, there is the form of security by way of general debenture, usually over all the assets of a company, including its stock in trade. Where a financing is of this kind, the situations in which the powers of the security holder to take possession, sell the assets subject to the debenture charge, or appoint a receiver are exercised, are clearly very different from those in which like power is exercised in relation to a mortgage of land or of a single chattel, such as a motor vehicle. While land or a motor vehicle, if left untouched for a short time, may not deteriorate significantly, a business will usually require immediate management and, if it involves wholesaling or retailing, a mortgagee in possession or a receiver will immediately be exercising power of sale in relation to items of stock in trade.

334 The range of securities and situations relating to personal property makes it unrealistic to attempt in any comprehensive way to confer powers or impose restrictions in relation to all personal property security interests. It also must be borne in mind that the Property Law Act is a statute of a general nature, the provisions of which should be applicable to all interests of a similar type. Where powers

or restrictions are thought necessary in relation to particular situations, such as for the purpose of consumer protection, it is the Law Commission's view that those should be found within statutes which are concerned with such matters. The Hire Purchase Act 1971, which will be mentioned below, is an example. We are therefore confining our proposals to powers and controls which can be made generally applicable and are concerning ourselves with mortgages or charges, leaving other forms of financing to be dealt with elsewhere, if that is thought necessary. It is assumed that the Hire Purchase Act will continue in force.

335 There would seem to be little advantage, even if it were practical, in legislating in a general way for securities over assets which are not goods or land.

Mortgagee in possession of goods

336 In using the word "goods" we have in mind the definition of it which appears in the draft Personal Property Securities Act (PPSA) which accompanied our Report No 8: A *Personal Property Securities Act for New Zealand* (1989). In this definition "goods" are all tangible personal property other than chattel paper, documents of title, negotiable instruments, securities and money (all of which are also there defined). It includes crops and the unborn young of animals but does not include trees until they are severed or petroleum or minerals until they are extracted.

337 Our preliminary view is that the proposed new Act should include a section stating that, upon default by a mortgagor of goods, the mortgagee may:

- take possession of the goods peacefully (ie, without committing forcible entry in breach of section 91 of the Crimes Act 1961) by physically taking possession; or
- (where the goods are in the possession of any third party) require payment direct to the mortgagee of any rental or other payments due by the third party to the mortgagor in respect of the goods; or
- bring proceedings seeking an order for possession.

(This section would be in parallel terms to one which we describe in para 285 for land mortgages.)

338 It could also be provided that possession by a mortgagee could be taken of goods which are equipment (as defined in PPSA) on the mortgagor's premises by rendering them unusable without removal. This suggestion is drawn from the PPSA legislation in some of the Canadian provinces.

339 In the great majority of cases, powers such as those above set out, and in much more extensive form, will have been conferred by the security documentation. On occasion the

statutory power may be useful. More importantly, the section would impose a requirement that the powers cannot be exercised unless there is default. Contracting out of this requirement would not be permitted. Possibly there may be circumstances in which a mortgagee might legitimately seek to take possession of goods before any default has actually occurred. We are inclined to think not; but, if submissions indicate that we are wrong in this view, it would be possible to include in the statute a right for a mortgagee to apply to the court for permission to seize mortgaged goods in such circumstances.

A "section 92" provision for mortgages of goods

340 There is no statutory requirement that prior notice be given before enforcement of a security by a mortgagee of goods. This contrasts with the position in relation to land mortgages (see para 286). Because of the nature of goods, some of which may be fragile or likely to depreciate quickly in value, it does not seem appropriate to require, in a statute of a general nature, prior notice before a mortgagee seizes the goods, though we observe that the PPSA legislation in Canadian provinces does contain such a requirement. We have also noted that section 26 of the Hire Purchase Act requires 10 days' notice of default to be given to the purchaser before goods can be repossessed. However, that is legislation of a consumer protection kind, limited in its application to sales at retail. A requirement for prior notice could result in hardship if imposed upon a holder of a debenture over a trading company which has stock in trade, although the debenture holder can appoint a receiver, rather than exercise any rights as mortgagee. It seems to us that cases of abuse can be controlled under the Credit Contracts Act 1981 or, sometimes, by reference to the mortgagee's duty to take reasonable care in selling mortgaged assets.

341 On the other hand, it seems to the Commission that, while a mortgagee of goods should, after default, be able to enter into possession without notice, there would be no hardship to a mortgagee in a general rule requiring a short period of notice (say, 7 working days, the rough equivalent of the 10 days in the Hire Purchase Act) before exercise of power of sale or the calling up of moneys under an acceleration clause. The notice would give the mortgagor a last opportunity of avoiding these consequences of default.

342 However, in certain situations, such a requirement would, we think, be inappropriate or unreasonably restrictive. Therefore we suggest that it should not apply to exercise of a power of sale of goods:

- by a receiver;
- in respect of perishable goods;
- where the goods are stock in trade sold at retail in the ordinary course of business;

- in respect of goods which, because of their condition or because of market conditions, are likely to decline substantially in value if not disposed of immediately;

- where the cost of care and storage of the goods is disproportionately large relative to their value; and

- where, after the default, the mortgagor consents in writing to the immediate disposition of the goods.

343 The Canadian legislation (from which we draw the exceptions) does not require the giving of such a notice by a receiver where the debtor is a corporation "the directors of which have ceased to have power to act because of the appointment of a receiver - manager". This reinforces our conclusion that a receiver should be exempted from the requirement of notice, but also retains the technical distinction between a mortgagee in possession and a receiver (the latter being the agent of the mortgagor/grantor). Receiverships commonly involve complicated commercial situations in which time may be of the essence in relation to decisions to sell. Entry into possession usually does not. However, a new section could contain authorisation for a mortgagee in possession to apply summarily to the court for dispensation from the requirement that a notice be given before sale.

Notice to guarantor

344 Except where a notice is not required to the mortgagor, we think that notice should have to be given to a guarantor of the debt before exercise of power of sale. This parallels the provision we suggest in relation to land.

Expiry of notice

345 We have suggested (in para 299) that a mortgagee's notice to a mortgagor of intention to sell up land should become stale after 12 months. We have a similar view here but suggest for consideration a period of six months. The difference reflects our perception of the relative volatilities of the two situations.

Questions:

Q72 **Should it be possible to take possession of equipment in the mortgagor's possession by rendering it unusable?**

Q73 **Should the court be empowered to allow a mortgagee to take possession of goods before there is a default by the mortgagor?**

Q74 **Should a mortgagee of goods be obliged to give a section 92 type notice before selling them or calling up the loan under an acceleration clause?**

Q75 **Should this be required before the mortgagee seizes possession?**

Q76 **If a notice is required, what exceptions should be recognised? (See our list in para 342.)**

Q77 **Should such a notice become stale after six months?**

XI
MORTGAGES OF PROPERTY GENERALLY

TACKING OF FURTHER ADVANCES TO LEGAL MORTGAGE

346 There are five forms of tacking, the first three of which appear to be inapplicable to Land Transfer land "at least as regards registered mortgages" (Hinde McMorland & Sim at para 8.078). These three categories are:

- tacking known as *tabula in naufragio* (the "plank in the shipwreck");
- ordinary tacking; and
- tacking further advances by virtue of the legal estate.

347 Each involves a person who has or acquires a legal mortgage and who also has an equitable mortgage, seeking to claim priority over an equitable mortgage which is intermediate between that person's two mortgages. In each situation the person seeking to tack must have had no notice of the existence of the intermediate mortgage at the critical time. In the first situation (*tabula in naufragio*) the claimant, having taken a third (equitable) mortgage without notice of the second mortgage, could acquire the first (legal) mortgage and tack the third mortgage on to it so as to squeeze out the second mortgage. Where the equities were equal as between the second and third mortgages because of the third mortgagee's lack of notice and where, apart from the time of their creation, the equities between the mortgagees were equal, the owner of the legal estate had priority.

348 The second category - ordinary tacking - occurs under the general law when a first mortgagee acquires a later equitable mortgage without notice of an intervening mortgage and can tack the later mortgage on to the first mortgage.

349 The third category involves a legal mortgagee, whose mortgage is without a "further advances" clause, making a further advance on the security of the legal estate without notice of the existence of a subsequent mortgage. In this situation further advances are agreed upon between the first mortgagee and the mortgagor after the second mortgage has been created. It is only at that time that the first mortgage is constituted as a security for further advances.

350 In each of these situations the right to tack is dependent on possession by the first mortgagee of a legal mortgage. However, under the Land Transfer system a memorandum of mortgage is merely a charge, albeit, by statute, a legal charge. These forms of tacking seem to have no application to Land Transfer land. They do not appear to be relied upon by mortgagees: there has been no caselaw in New Zealand in which the question has been considered.

351 There would seem to be little reason to preserve these rules of tacking which depend upon possession or acquisition of a legal mortgage and we propose recommending their abolition.

Question:

Q78 Should any of these forms of tacking be preserved?

CONTRACTUAL TACKING

352 The forms of tacking just considered all involve possession of a legal mortgage by the mortgagee who wishes to tack. However, the kinds of tacking commonly found in New Zealand do not depend upon possession of a legal mortgage. Contractual tacking and tacking by virtue of section 80A of the Property Law Act 1952, which facilitates contractual tacking, can occur regardless of whether the mortgage in question is registered or unregistered. The mortgage document itself provides that it will secure further advances (as defined in the mortgage or by reference to the definition found in the Fifth Schedule of the Chattels Transfer Act 1924). A trading bank mortgage provides a typical example of an arrangement for contractual tacking.

353 But immediately the holder of a current account mortgage of this kind learns that the mortgagor has later executed a mortgage over the same property in favour of a third party, the rule known as the rule in *Hopkinson* v *Rolt* (1861) 9 HL Cas 514; 11 ER 829 comes into operation. That case determined that any advances made by the prior mortgagee after notice of the existence of the subsequent mortgage rank in priority behind the subsequent mortgage except in circumstances in which the first mortgagee is compelled to make those further advances, such as where a banker has already established a letter of credit on behalf of the mortgagor in favour of a creditor of the mortgagor and cannot refuse to honour the letter of credit (*Westpac Banking Corporation* v *Ellice Properties Ltd* (1991) 1 NZ ConvC 190,718). It is notorious that, by virtue of the operation of the rule in *Clayton's Case* ((1816) 1 Mer 529, 572; 35 ER 781) that the first receipt from borrower pays the earliest advance, the prior mortgagee gradually concedes priority to the subsequent mortgagee even though the amount owing under the prior mortgage is not increased or may even diminish. The combination of these two rules in such circumstances is commercially unreal and may work very unfairly.

354 Section 80A of the Property Law Act is an attempt, only partially successful, to provide a means by which, up to a limit agreed to by the parties to the first mortgage, the first mortgagee can make further advances irrespective of notice of the existence of a subsequent mortgage. Subsection (1) is concerned with the relatively simple situation in which there is to be an advance of a certain sum by progress payments (often for the purpose of funding building

operations) but it is not intended that, once that sum has been advanced, there are to be any further advances: there is no current account. The subsection requires that the amount to be advanced be specified in the mortgage. Provided that is done, advances by instalments up to that amount rank in priority to a subsequent mortgage even if notice of it is given to the prior mortgagee. But there is no priority for amounts which are repaid and readvanced after notification of the subsequent mortgage.

355 Although subsection (1), with its relatively simple function, is adequate for its purpose, there has been widespread discontent with subsection (2), which deals with advances on current account. The subsection states that it is lawful to specify in a current account mortgage a maximum amount to rank in priority to any subsequent mortgage. Where that is done, the mortgage takes effect accordingly notwithstanding anything in any rule of law to the contrary and notwithstanding that the sum owing under the mortgage includes amounts repaid and readvanced. The maximum amount may be varied but no increase is binding on a subsequent mortgagee existing at the time of the variation unless that person has consented. Subsection (3) similarly provides priority to the mortgagee for moneys required to be paid under a guarantee and secured by mortgage where the payment is made after notice of a subsequent mortgage.

356 Section 80A(2) presents difficulties of two kinds. First, it is badly drafted. There is uncertainty about:

- The way in which a priority limit can be stated - whether it can be in foreign currency and whether it must be one sum or one sum plus interest on that sum and expenses of realisation.

- Whether "advances" is a wide enough term to cover the variety of financial accommodation normally secured by mortgages and other securities taken by financiers. It is uncertain whether it includes payments made or obligations undertaken to a third party.

357 These drafting difficulties can relatively easily be corrected. But the second problem is, at the time of writing, harder to overcome. It relates to the question of notice of the priority limit, including any variation. Unfortunately section 80A is not interrelated with the Land Transfer Act, the Chattels Transfer Act, the Companies Act 1955, the Shipping and Seamen Act 1952 or any other present system of registration of security interests. So it is possible, at least in theory, for a priority limit to be stated in a first mortgage of, say, a mortgage of shares, but to remain invisible because that mortgage is incapable of registration. Even if it were registrable, the fact that it remained unregistered might not prevent the operation of the section. There seems to have been no caselaw on this question.

358 Moreover, unless equity is able to come to the rescue by use of estoppel or some other equitable device, a priority limit could be "secretly" increased and a future second mortgagee affected by that increased limit despite the fact that the original lower limit was the only priority stated in the registered document. It should be noted that there is no provision in the Companies Act, the Chattels Transfer Act or the Shipping and Seamen Act for registration of a variation of this kind.

359 At the time of writing this paper, the Law Commission does not know whether its Report No 8: *A Personal Property Securities Act for New Zealand* (April 1989) and the draft Bill attached to that report, is to be translated into legislative form. If so, it would replace Part IV of the Companies Act (which requires registration of company charges) and the Chattels Transfer Act. The Companies Bill now before Parliament contains no provision for registration of company charges as it is based on the work of the Commission (Reports Nos 9 and 16) which assumed that there would be a Personal Property Securities Act (PPSA). The latter provides a comprehensive system for notification onto a central computerised register of the existence of security interests of all kinds, including mortgages and charges, given by individuals and corporations over personal property. Registration of mortgages over land would then be solely under the Land Transfer Act (no provision being made anywhere for registration of charges solely over unregistered interests in land - although general charges, debentures, would be registered under PPSA) and ships' mortgages would still be registered under the Shipping and Seamen Act. An amendment to the latter Act would be necessary to enable registration of variations of mortgages, including priority limits.

360 With these legislative alterations in place the difficulties that presently arise concerning unregistrable charges, such as mortgages of shares, will very substantially diminish. Unregistered interests in land are only rarely of any real significance as security interests.

361 PPSA has been adapted from a North American model. It has been in widespread use in the United States of America and Canada for many years. One of the provisions which has been drawn from that model is section 28(2)(c) of the Law Commission's draft which negates the rule in *Hopkinson* v *Rolt* for transactions registrable under PPSA. That subsection states that priority of all advances made pursuant to a security interest is to be the same. It is ordinarily determined by the time of registration (section 28(1)). This is, of course, subject to any agreement which may be reached between the holders of security interests.

362 It would be anomalous if mortgages of personal property (other than registered ships) were to be governed by one rule and mortgages of land and registered ships by another. The Commission has provisionally concluded that abolition of the rule in *Hopkinson* v *Rolt* is the simplest solution to the current problems with section 80A. The rule is out of touch

with modern commercial practices. This is, we believe, one of the reasons why it was dispensed with in North American versions of PPSA. When the rule in *Hopkinson* v *Rolt* was developed there were no security registration systems nor any statutory controls on the behaviour of mortgagees. If the rule did not exist a first mortgagee would not have had to take any notice of the existence of subsequent mortgages and could simply have continued to tack advances of all kinds contemplated by the first mortgage document. The subsequent mortgagee might have no knowledge of the existence of the first mortgage and no means of obtaining any details of it once he discovered its existence. There was no requirement for any public notification in order that a claim for priority could be made.

363 We have also taken notice of the manner in which priority arrangements are ordinarily made between mortgagees in New Zealand financial markets. Having ascertained the existence of a first mortgage, a person who intends giving financial accommodation to the mortgagor will, with the co-operation of the mortgagor, approach the mortgagee (where the mortgage secures further advances) and negotiate a priority limit beyond which further advances under that mortgage will rank in priority behind those of the intending second mortgagee. If the first mortgage is registered and contains a priority limit, the second mortgagee might possibly rely upon that fact, although it would be dangerous to do so because of the possibility of a variation having already been agreed but not registered. However, many financial institutions, including the trading banks, do not take advantage of section 80A because of its deficiencies. A typical bank mortgage on public register reveals the existence of the mortgage and the identity of the lender but contains no information from which the intending second mortgagee can discover the amount which has been advanced or is intended to be advanced thereunder. It is therefore commonplace that the second mortgagee, as will be the case under PPSA, must approach the first mortgagee and obtain this further information, at the same time reaching agreement upon the priority limit which will apply. A deed of modification of priority is then executed by the mortgagor and the two mortgagees. The document always contains a statement negating the effect of the rule in *Hopkinson* v *Rolt*.

364 It is unusual to find a question of priority between an existing current account mortgagee and an intending mortgagee handled in any manner other than the one just described. The Commission is therefore confident that abolition of the rule in *Hopkinson* v *Rolt* would not involve any change in the practices of lenders of money but would, in fact, bring the law into line with those practices - as well as aligning the law relating to mortgages of land with that to apply to mortgages of personal property if PPSA is enacted.

365 The Law Commission has considered whether, if the rule in *Hopkinson* v *Rolt* is abolished, a first mortgagee might take security over all the assets of the mortgagor and then "hog" that security by refusing to agree to any priority limit. This might make it impossible for the mortgagor to raise funds

by a second mortgage from another lender. In practice, a variant of this behaviour could already occur under the existing law: the first mortgagee could simply insert in the documentation an unnecessarily high priority limit. But our observation is that this abuse does not occur; certainly it has not come to our attention. The probable reason, apart from the commonsense of most of those who operate in financial markets, is that the court is empowered to reopen an oppressive credit contract by virtue of section 10 of the Credit Contracts Act where such a contract, or any term, is oppressive or a party under the contract has exercised or intends to exercise a right or power conferred by the contract in an oppressive manner. It seems to us very likely that a court would readily reopen the first mortgage contract if the first mortgagee oppressively "hogged" the security and would make an appropriate order under section 14 of that Act requiring the first mortgagee to agree to a reasonable priority limit. Nevertheless, if it is felt that there is any doubt on this point, the Credit Contracts Act could be amended to empower the court specifically.

Questions:

Q78 Should the rule in *Hopkinson* v *Rolt* be abolished?

Q79 If so, does the Credit Contracts Act provide sufficient protection for mortgagors and intending subsequent mortgagees?

REDEMPTION AND DISCHARGE OF MORTGAGES

366 The sections in the 1952 Act concerned with redemption are sections 81 to 87. It seems that sections 85, 86 and 87 apply to mortgages of both real and personal property. For reasons not apparent to us, section 81 does not: it refers to "mortgaged land" (although it extends to mortgages "comprising both land and chattels": section 81(6)). Compare section 86 which speaks of "mortgaged property". Because sections 82 and 83 are supplemental to section 81, they do not apply to personalty (*Schollum* v *Maxwell* (1914) 33 NZLR 1407; *Equiticorp Finance Group Ltd* v *Cheah* [1991] 1 NZLR 299, 302). The Commission sees no good reason for the distinction and suggests that all of the sections concerned with redemption should apply to mortgages and charges of all kinds of property.

Compensation for early repayment

367 Section 81 states the basic rule that a mortgagor is entitled to redeem at any time before the subject matter of the mortgage has been actually sold by the mortgagee under the power of sale upon payment of all money due and owing under the mortgage at the time of payment. Section 81(2) gives the mortgagor a right of redemption although the time for redemption appointed in the mortgage has not arrived "but in that case he shall pay to the mortgagee, in addition to any other money then due and owing under the mortgage, interest on the principal sum secured thereby for the unexpired portion of

the term of the mortgage". This statement must be read in light of, and is mitigated by, sections 10 and 11 of the Credit Contracts Act. Section 10(1) enables the court to reopen the contract where a party is exercising its powers in an oppressive manner. Section 11(2)(b)(iii) requires the court to have regard to whether the creditor has required payment of interest of "oppressive" amount for a period subsequent to the date of an early repayment. The court must consider the expenses of the creditor and the likelihood that the amount repaid can be invested on similar terms. In *Cambridge Clothing Co Ltd* v *Simpson* [1988] 2 NZLR 340 the mortgagee was insisting on receiving six months' interest because the mortgagor was exercising the right of early redemption. The court held that this was not necessarily oppressive behaviour on the particular facts of that case and remitted it to the District Court for further consideration of the point. In contrast, in *National Westminster Finance New Zealand Ltd* v *United Finance & Securities Ltd* [1988] 1 NZLR 226, Smellie J thought that there was an 80 per cent likelihood that the Court would strike down a provision requiring payment of three months' penalty interest in circumstances where a receiver had sold the property and the first mortgagee had immediately re-lent the principal sum, apparently at the same ordinary interest rate.

368 We have considered whether a new version of section 81 should impose a limit on the amount of "penalty" or "bonus" interest chargeable upon an early repayment. We had in mind the equivalent of six months' interest, it being our understanding that it is unusual for a mortgagee to demand more than this. Indeed, some institutional mortgages contain provision for early repayment without stipulating for *any* penalty. And, as noted in the last paragraph, the Credit Contracts Act already regulates attempts to charge any amount of penalty interest which would be contrary to "reasonable standards of commercial practice". We would be interested to learn how this provision is working in practice.

369 But we have tentatively concluded that it would be wrong for the Act to impose a rigid limit on the amount of penalty interest which a mortgagee can require. The maximum might become the minimum (although this could be overcome by a statement that penalty interest must be reasonable in the circumstances). A more serious objection is that a limit might unfairly deprive a mortgagee of its bargain, particularly where it had accepted or been saddled with a rate below the market level and the mortgagor sought to repay as soon as interest rates in the market declined below the rate being paid on the mortgage. However, the factor which weighs most heavily with the Commission is that section 81 applies to all mortgage securities, including those which may be traded in a market where prices are calculated on the basis of yield to maturity. We suspect that such a market could not easily accommodate the risk that a mortgagor might at any time seek to repay, tendering, say, six months' interest. Nor should the rules applicable to repayments differ depending upon whether or not a tradeable instrument is secured over an asset of the debtor. The Credit Contracts Act applies to both secured and unsecured credit obligations and appears, in a

flexible manner, to provide sufficient safeguard against excessive demands for additional interest when early payment is made. It would be our expectation that the courts will in cases under that Act be able to develop a "rule of thumb" by which mortgagors can calculate how much penalty interest to tender in the majority of cases. We think, however, that the circumstances in the minority of situations are too various to be encapsulated in rigid statutory rules.

Mortgagee required to transfer

370 The right to redeem a mortgage is exercisable by anyone to whom a mortgagor grants rights in mortgaged property: a subsequent mortgagee or a debenture holder, a purchaser or even a lessee - as in *Tarn* v *Turner* (1888) 39 ChD 456. In that case an equitable lessee from the mortgagor wished to redeem the mortgage in order to be able to take possession of the premises as mortgagee in possession. Sections 82 and 83 of the Act give a mortgagor or anyone else with a right to redeem the mortgage the ability to require the mortgagee, instead of discharging the mortgage, to transfer it to someone nominated by the person wishing to redeem. This is useful if there is doubt about the right of the mortgagor to execute a new mortgage when a refinancing is occurring or if a subsequent mortgagee will not agree to priority for the replacement. The operation of sections 82 and 83 is described in *Teevan* v *Smith* (1882) 20 ChD 724 and *First Chicago Australia Ltd* v *Loyebe Pty Ltd* [1980] 2 NSWLR 703. "Mortgagor" has an extended definition in section 2. It includes anyone claiming title under the original mortgagor (a transferee of the land) and anyone entitled to redeem the mortgage. The reference in section 83 to a "third party" has been held to include any person seeking to redeem other than the mortgagor. In this context "mortgagor" should, we think, apply only to the current mortgagor.

371 The sections do not apply where a mortgagee is, or has been, in possession. That is because, if the mortgagee were forced to transfer the mortgage, it would not be released from liability to account as a mortgagee in possession. The mortgagee might be responsible for wilful neglect or default by the transferee unless the transfer was made by order of the court or with the mortgagor's concurrence (*Hall* v *Heward* (1886) 32 ChD 430), though no doubt the transferring mortgagee would be entitled to an indemnity from the transferee. Consequently, the exception should remain or the law relating to mortgagees in possession should be amended to exempt the mortgagee from continuing liability in these circumstances. We are inclined to recommend continuance of the existing exemption where the mortgagee remains in possession. We are, however, proposing (at para 314) that it should be made easier for a mortgagee to withdraw from possession and so avoid future liability for possession of the property. Once the mortgagee is out of possession, the right of redemption by transfer should revive. The Commission favours restatement of the sections in modern form with these minor alterations in their substance.

Court order for sale

372 The present relevance and meaning of section 86 (sale of mortgaged property in action for redemption) has become harder to discern as its origins have become more distant and the law relating to the right of a mortgagor to bring proceedings against the mortgagee has changed. Section 80B overturned the rule of law whereby the mortgagor was barred from instituting proceedings in relation to the mortgage against the mortgagee unless first offering to redeem the mortgaged land. (The work of abolition having been done, it will not be necessary to repeat that section in the new Act: section 20(e) Acts Interpretation Act 1924.) Because this rule has been abolished there appears no need to restrict section 86 to an action for redemption.

373 In England the section equivalent to section 86 acts as a control on the mortgagee's right to foreclosure (Megarry & Wade at 907-908) but this will not be relevant in New Zealand as foreclosure in respect of land has been abolished (section 89). However, a situation could arise where a mortgagor is in default but the mortgagee is taking no steps to exercise power of sale. The mortgagor may wish to sell the property to stop interest running but may be unable to sell because the amount which can be obtained on sale will be insufficient to repay the mortgage on the property. Alternatively, a subsequent mortgagee may wish to prevent further erosion of the mortgagor's personal position in circumstances in which the property is unlikely to yield sufficient to repay the prior mortgage. In such instances it may, very occasionally, be useful for the mortgagor or the subsequent mortgagee to have the right to seek a court order that the property be sold. (An example is found in *Brewer* v *Square* [1892] 2 Ch 111.) The right to make application to the court could be extended to a covenanting party. It will, we think, provide a balancing factor against the mortgagee's right to delay the time of sale (*China and South Sea Bank Ltd* v *Tan Soon Gin* [1990] 1 AC 536 (PC) and *Countrywide Banking Corporation* v *Robinson* [1991] 1 NZLR 75 (CA)).

374 Section 86(2) now gives the court the right to direct a sale of the mortgaged property upon request of the mortgagee or other interested person. It is proposed to restate section 86 to enable mortgagees, mortgagors, covenantors and others with a proprietary interest in or charge over the property (including persons holding unregistered mortgages) to apply to the court for an order for the sale of the property. The right of a mortgagee to apply should be preserved in case the mortgage documentation is defective or non-existent, as it was in *State Advances Corporation of New Zealand* v *Billingsley* [1942] NZLR 223 (mortgage by deposit of share scrip). Any new section would need to give the court power to require payment into court to meet expenses of sale and secure performance of terms and should contain ancillary powers as the existing section does.

Provisions for consolidation and where mortgagee unable to be found

375 The restriction on consolidation now found in section 85 does not seem to require any substantive change. Nor does section 87, dealing with the payment of money and the obtaining of a discharge from the court where the mortgagee is out of the jurisdiction, cannot be found, is unknown or is dead or it is uncertain who is entitled. However, the jurisdiction under the section could well be vested in the District Court.

Discharge of mortgages

376 Section 79 (inter alia) enables a mortgage to be discharged by a memorandum endorsed on or annexed to it and executed as a deed is required to be executed. A discharge can be effected in this manner for the purposes of the Land Transfer Act. Section 79(4) provides that "[e]very such memorandum of discharge shall vacate the mortgage debt". This wording can be contrasted with section 111 of the Land Transfer Act which refers only to the discharge of the land and does not assume repayment of indebtedness. Section 79(4) has led to considerable difficulty where a discharge has been executed but the mortgage debt has not been paid, perhaps because of a mistake on the part of the mortgagee (see *Perpetual Trustees Estate & Agency Co of NZ Ltd* v *Morrison* [1980] 2 NZLR 447 and *Marac Finance Ltd* v *Dyer* (unreported, High Court, Christchurch, 20 November 1989, CP 160/88), a decision of Holland J which is the subject of a commentary by Dr D W McMorland in (1990) 5 BCB 185).

377 The Commission believes that there should be no statutory rule that a discharge vacates the debt. Instead the Act should simply provide that the memorandum of discharge discharges the security and should leave the question of its effect on the debt to the general law. In *Broad* v *Public Trustee* [1939] NZLR 140 the court concluded that a discharge which was in the form of a deed necessarily estopped the mortgagee from asserting that any indebtedness remained. But that decision has been criticised by commentators, as is mentioned in Dr McMorland's article and is, we think, unlikely to be followed.

Questions:

Q80 **Should the redemption sections (sections 81-87) all apply to mortgages of all kinds of property?**

Q81 **Should section 81(2) prescribe a maximum amount of interest which may be demanded on early redemption?**

Q82 **Should a mortgagee, mortgagor, a covenantor or any other person with security over the property have the right to apply for a court order that mortgaged property be sold (as described in para 374)?**

Q83 **Should jurisdiction under section 87 (repayment when mortgagee cannot be found) be vested in the District Courts?**

XII
SALES BY MORTGAGEES THROUGH REGISTRAR OF HIGH COURT

Advantages of procedure

378 For over 130 years it has been possible for a mortgagee to apply to the court to conduct an auction sale of mortgaged land when the mortgagor has defaulted. The use of the Registrar's sale procedure has been thought to have two significant advantages for a mortgagee:

- the mortgagee can, if necessary, become the purchaser of the property (section 101); and
- the mortgagee is protected against an allegation by the mortgagor (or other interested party) that the sale has been at an undervalue.

379 The first of these advantages certainly remains and on its own would seem to provide substantial justification for retaining Registrar's sales. Although clause 8 of the Fourth Schedule to the Act appears to give the mortgagee "power to buy in the mortgaged property or any part thereof at any sale by auction", it seems that these words must, in the absence of clear statutory sanction (which clause 8 is not) and except in the case of a sale by the Court, have been intended to apply only to a sale through the Registrar, for "[a] sale by a person to himself is no sale at all" (*Farrar* v *Farrars, Ltd* (1888) 40 ChD 395, 409, Lindley LJ).

380 The second advantage has probably already been very substantially eroded by developments in the law relating to the liability of mortgagees. The courts in New Zealand have accepted the position arrived at by the Court of Appeal in England in *Cuckmere Brick Co Ltd* v *Mutual Finance Ltd* [1971] Ch 949 in which it was found that a mortgagee who neglected to advertise adequately the auction of the mortgaged property was liable to the mortgagor for the loss consequently suffered by the latter. It can be persuasively argued that resort to the Registrar will not absolve a mortgagee who has been guilty of some negligent act in relation to the sale (S Dukeson [1988] NZLJ 325). The Companies (Ancillary Provisions) Bill now before Parliament will, if enacted, add to the Property Law Act a new section 103A requiring a mortgagee who exercises a power of sale of mortgaged property, "including exercise of a power of sale through the Registrar" under section 99, to take reasonable care to obtain the best price reasonably obtainable as at the time of sale. This will, in effect, put into statutory form the *Cuckmere Brick* rule and will extend it to a mortgagee selling through the Registrar. (It does not appear that the Registrar will be placed under a new obligation by the section.)

Should Registrar's sale be abolished?

381 Representations have been made to us by practitioners well known for their expertise in relation to the law of mortgages that the device of the Registrar's sale should now be done away with and that, subject to certain controls, a mortgagee should be permitted to buy in at any sale by public auction. It is argued that there should be a provision requiring a reserve price - equivalent to the mortgagee's estimate of the market value of the property - to be fixed and also requiring that all details of the auction, including the reserve price, must be advised to the mortgagor and other interested parties at least a month ahead of the auction date. However, the Law Commission observes that the Registrar plays a valuable role in providing independent supervision of the conduct of the sale. The Registrar approves the conditions of sale and the advertising, checks that the power of sale has indeed become exercisable and that section 92 has been complied with, appoints the auctioneer, receives a report from the auctioneer after the sale and, if the mortgagee buys in, executes the memorandum of transfer. We do not think that, in relation to a sale at which the mortgagee may buy the property, these controls should be removed unless they are replaced by some other, equally reliable, independent vetting of the conduct of the sale. The present Registrar's sale system - particularly the advertising - may leave something to be desired by modern commercial standards but the Commission, while very interested to receive submissions on it, is cautious about recommending that it be abolished.

Chattels

382 Section 46 of the Chattels Transfer Act 1924 applies sections 99 to 103 of the Property Law Act "with the necessary modifications" to chattels. It seems that it is rarely (if ever) used. None of the Registrars of the High Court who responded to our request for information had ever encountered an application in respect of a chattel. But there still seems to be no good reason for excluding chattels from sales by Registrars. It is possible that a mortgagee might have security over both land and associated chattels and might wish to sell them together, at the same time being in a position to buy in. The Commission's Report No 8, *A New Personal Property Securities Act for New Zealand*, recommended upon repeal of the Chattels Transfer Act a new section 99A to make sections 99 to 103 applicable to collateral (as defined in PPSA).

Redemption price

383 Some criticism has been made of the concept of the redemption price. Section 99(1) requires the mortgagee in the application to the Registrar to state the price at which the mortgagor may redeem the land to be sold. Before an amendment in 1982, the sum nominated by the mortgagee was known as the mortgagee's "estimate of value". That term was found to be confusing because, if the property was worth more than the amount owing under the mortgage, the mortgagee would not

be estimating the value of the property, but indicating the lower amount needed to be found by the mortgagor to discharge the mortgage. Because the mortgagee might buy the property at the auction, and the estimate of value would then become the purchase price payable by the mortgagee (unless the mortgagee bid higher than the estimate), it was not sensible to state an estimate of value which was greater than the amount which would be outstanding under the mortgage when the time came for settlement.

384 Unfortunately the term which was adopted in 1982, "redemption price", is equally (and doubly) misleading since a payment by the mortgagor is neither a redemption (as the mortgagor has remained the proprietor of the legal estate throughout, the "mortgage" being merely a charge) nor a price (though it may become the consideration payable by the mortgagee: section 100). It has recently been confirmed that there is no direct relevance between the redemption price and the amount due and owing under the mortgage (*NZI Finance Ltd* v *Westpac Finance Ltd* (1991) 1 NZ ConvC 190,788). The Commission thinks that it may be helpful if there is a further change of terminology. It is suggested that the section should require that the application be made in writing and that it "nominate the sum upon payment of which the applicant agrees to discharge the mortgage insofar as it relates to the property in respect of which the application is made". The section could define that sum as the "nominated sum". That term would then be used in the sections permitting "redemption" by the mortgagor and permitting the mortgagee to become the purchaser.

385 The Commission understands that there is sometimes confusion over whether, when the mortgagee who applies to the Registrar is a second mortgagee, the redemption price (our "nominated sum") should include an amount sufficient to repay the first mortgage. Clearly it should not: section 104 of the Land Transfer Act 1952, which governs the application of purchase money after a sale by a mortgagee, makes no provision for the application of purchase moneys in payment of a prior mortgage. The second mortgagee should, therefore, sell subject to the first mortgage, though it would usually be prudent to point out to intending purchasers that the first mortgagee may well require repayment. That is a question of conveyancing procedure which seems best left to be handled by the mortgagee in the drafting of the conditions of sale. The nominated sum would continue to be left to the discretion of the applicant mortgagee but, unless the property is considered to have a lower value, it would normally be the amount which the property will "owe" the applicant by the time of the sale. This will include any amount paid to the prior mortgagee by the applicant to remedy a default under the prior mortgage, unless the prior mortgage is then transferred to the applicant, but will not otherwise take the prior mortgage into account. The applicant is not concerned with the state of accounts between the mortgagor and the prior mortgagee if the applicant's mortgage is paid out and, if the applicant buys the property at the auction, he or she will take it subject to the prior mortgage and therefore should not have it included in the amount for which allowance must then be made to the

mortgagor. We hope that this point may be brought into better focus by changing the language of section 99 as we have indicated.

386 The Commission understands that some Registrars take the view that only one redemption price can be stated in the application, even when it is intended to offer the mortgaged property in separate lots. The purpose of the redemption price, particularly its function as the consideration when the mortgagee is the buyer, suggests that this interpretation cannot be correct. A mortgagee who purchases part of the land is surely not obliged to pay or allow a consideration related to the whole. Nevertheless it would clarify the point if it were stated that separate sums may be nominated for different parts of the security.

Date of application

387 There would also be advantage in defining the date of the application as the date on which the completed application is filed with the Registrar. This would answer the point left unanswered in *Hampton* v *The Registrar of the High Court at Auckland* (1990) 1 NZ ConvC 190,559.

Fixing of date of auction

388 Section 99(2)(a) requires the Registrar to fix a "convenient time" for the auction "being not more than three months and not less than one month from the date of the application". While we see no reason to vary the minimum period, we think that the maximum should be extended to at least six months or abolished altogether. We understand that it can cause timing difficulties if an application is made before Christmas. It seems to serve no useful purpose. Any undue delay by the Registrar could be dealt with by an application to the court for an order that a sale date be fixed.

Advertising

389 Section 99(2)(c) requires the Registrar to "[g]ive such notice of the sale by advertisement in a newspaper circulating in the neighbourhood as he considers sufficient". The Registrar requires the notice to be inserted at least twice, but the form of notice usually approved is very formalised and often bears little resemblance to the kind of advertising normally adopted by those wishing to sell their own properties. It may be difficult to prescribe a form of advertisement avoiding the kind of formality which may deter a casual reader. Registrars would not wish to have responsibility for approving advertisements containing puffery or real estate jargon. But the Commission would like to see mortgagee sale advertising, where the sale is conducted by the Registrar, placing greater emphasis on the address and physical characteristics of the property and less on the detail of the legal description and mortgage number. We note from perusal of public notice columns that this practice is increasing in private mortgagee sales advertising.

390 The reference in section 99(2)(c) to a newspaper circulating "in the neighbourhood" should also, we believe, be amended to enable the Registrar to direct more extensive advertising where this is appropriate. It may be that in certain cases the special characteristics or value of a property requires that it should be advertised throughout New Zealand or even overseas. The Registrar should have power to direct this. It should also be possible (and this is really required by the developing caselaw and prospective legislation on the obligation of the mortgagee to obtain the best price reasonably obtainable in the circumstances) for the mortgagee to be able, in its discretion, to carry out more extensive advertising and other marketing of the property with the cost reasonably incurred in doing so being claimable as an expense incurred by the mortgagee incident to the sale or any attempt at sale. Perhaps the court should have express power to overrule the directions of the Registrar and require additional advertising or other marketing.

Reserve price

391 One of the more unusual features of a Registrar's sale is that the Registrar is given no power to fix a reserve price nor to authorise the fixing of a reserve by the mortgagee. Indeed, this practice is forbidden (*Public Trustee* v *Wallace* [1932] NZLR 625). Possibly the reason for this is that, if a Registrar were to be empowered to fix or approve a reserve price, the Registrar might thereby be exposed to potential negligence claims alleging that either the Registrar should have fixed or approved a reserve price and failed to do so, or that a reserve fixed or approved was too low and that loss had consequentially been suffered by the mortgagor. There may also be some reluctance to impose upon the mortgagee the burden of obtaining a valuation to substantiate a reserve price.

Withdrawing the property

392 However, Registrars regularly approve conditions of sale which give the vendor the right to withdraw the property from sale before it is actually sold. In this way the mortgagee can impose an unofficial reserve without the consequence of exposing the Registrar to liability. It does not appear that this practice has led to any abuse. If it has, we have not been made aware of it as a result of our inquiries. The Commission suggests that to put to rest any doubt that a power for the mortgagee to withdraw the property is inconsistent with *Public Trustee* v *Wallace*, a section in the new Act should expressly authorise it. While this might be seen as taking some of the control of the sale out of the hands of the Registrar, it would ensure that the law is consistent with current practices and would not, it seems, prejudice any mortgagor. However, we think that the section should also provide that the Registrar may disallow any expense incurred by the mortgagee in relation to an abortive auction where the mortgagee has acted unreasonably. In that circumstance it should not be possible for the mortgagee to claim the expense as a sum which is reimbursable. Possibly,

also, the right to withdraw should not be exercisable once the redemption price has been reached in the bidding, though, for the present, we are hesitant about this last point.

393 It has been noted above that one of the functions of the Registrar is to investigate whether the mortgagee is entitled to exercise the power of sale. That ought to be made more explicit in the legislation. The Commission thinks that the Registrar should be given express power to withdraw the property from sale if at any time it is believed that there has been an irregularity or impropriety, and that the sale is not being properly conducted (see *In Re Prestidge* (1989) 1 NZ ConvC 190,244). The Registrar could also be given power to correct or allow correction of defects and errors in the application or ancillary documents.

Questions:

Q84 **Should mortgagees continue to have the option of applying to the Registrar of the High Court for the sale of mortgaged land upon default by the mortgagor?**

Q85 **If so, should the process be available also in the case of mortgages of goods?**

Q86 **If sales through the Registrar were to be abolished, should mortgagees be permitted to buy in and, if so, under what circumstances and with what (if any) independent control?**

Q87 **Should the "redemption price" be renamed? Is "nominated sum" an appropriate term?**

Q88 **Should the requirement for a sale date to be within three months of the mortgagee's application be abolished?**

Q89 **What amendments should be made to the advertising requirements in relation to mortgagee sales?**

Q90 **Should the court have power to override the directions of the Registrar and require additional advertising or marketing of the property?**

Q91 **Should there be a reserve price at an auction conducted through the Registrar?**

Q92 **Should the mortgagee (and the Registrar) have power to withdraw the property from sale at or before such an auction?**

Q93 **Should the right of withdrawing the property from sale be available after the bidding has reached the redemption price?**

PART D: LEASES OF LAND

XIII
COVENANTS IN LEASES

IMPLIED COVENANTS AND POWERS

Common law covenants

394 The situation concerning the covenants implied in a lease is now both complicated and uncertain. At common law it was found necessary to imply certain covenants by the landlord and the tenant in order to make the grant of a lease effectual. The covenants implied by the common law are:

Covenants by the tenant

- to pay rent
- to pay rates and taxes (except such of them as fall on the landlord by statute)
- not to commit voluntary waste
- to use the premises in a tenant-like manner
- to permit the landlord to enter and view the premises (where the landlord is liable to repair them)

Covenants by the landlord

- for quiet enjoyment (in limited form)
- not to derogate from the grant.

Usual covenants

395 These covenants are implied into a lease of land at common law when a landlord, without having entered into any preliminary agreement to lease, simply grants possession of the premises to the tenant for a certain term and rent. But when there is a prior agreement, the common law implies that the parties have agreed to include in the lease what are called "usual covenants". These are in addition to and modification of the common law covenants. The lease is subject to an implied condition that the landlord may re-enter if the tenant fails to pay the rent and the tenant's covenant to use the premises in a tenant-like manner is expanded to a covenant in unqualified form to keep the premises in good repair and deliver them up in this state at the end of the term.

Covenants concerning condition of premises

396 A tenant liable merely to use the premises in a tenant-like manner has limited obligations only. ("Husbandlike" has the same meaning and is sometimes used in

farming leases.) They are described by Denning LJ in a well-known passage in *Warren* v *Keen* [1954] 1 QB 15, 20:

> The tenant must take proper care of the place. He must, if he is going away for the winter, turn off the water and empty the boiler. He must clean the chimneys, where necessary, and also the windows. He must mend the electric light when it fuses. He must unstop the sink when it is blocked by his waste. In short, he must do the little jobs about the place which a reasonable tenant would do. In addition he must not, of course, damage the house wilfully or negligently; and he must see that his family and guests do not damage it, and if they do, he must repair it. But, apart from such things, if the house falls into disrepair through fair wear and tear or lapse of time, or for any reason not caused by him, then the tenant is not liable to repair it.

397 With appropriate modification this statement gives some guidance in relation to tenancies of non-residential properties. (Section 142 of the Residential Tenancies Act 1986 excludes the application of Part VIII of the Property Law Act, which includes sections 106 and 107 to residential tenancies.)

398 In contrast to the common law obligation to use the premises in a tenant-like manner, the "usual" covenant implied at common law where there is an agreement to lease is a full repairing covenant with no qualification exempting the tenant from damage caused by fire or other perils or deterioration falling within fair wear and tear.

Statutory covenants

399 Superimposed upon these common law and usual covenants are sections 106 and 107 which imply into every written lease certain optional covenants (lessee's obligation to pay rent and keep premises in repair, lessor's powers to enter and inspect, to re-enter for breach and to levy distress). Consequently there is uncertainty about whether a reference in an agreement to lease to "usual covenants and conditions" (or similar language) will be found to be a reference to sections 106 and 107 or to "usual" covenants at common law. As a third possibility, the expression may be found in particular instances to be a means of invoking covenants which go beyond common law and statute, but are commonly found in the leases in use in a particular part of New Zealand or a particular trade or business. It is beyond the capacity of legislation to avoid doubts whether this third class of "usual" covenants is intended; but it is possible to ensure that the common law implied and usual covenants are completely replaced by the statutory covenants. We envisage in the proposed new Act a statement that, except as provided in the Act, no covenant shall be implied as a matter of law in any lease and a further statement that reference to "usual covenants" in any document is to be taken to be a reference to the implied covenants in the Act unless the context requires otherwise.

400 There is also uncertainty whether the statutory covenants apply in the case of an oral tenancy. Probably not: the recent decision of Tompkins J in *Chapman* v *Moray Industries (1986) Ltd* (1991) 1 NZ ConvC 190,700, although on a different point, seems to confirm a restrictive view. So does the existence of a definition of "lease" in section 117, applying to sections 109, 110 and 118-119 only. If the statutory covenants apply to equitable leases they do so only because of the operation of the rule in *Walsh* v *Lonsdale* (1882) 21 ChD 9 (see F M Brookfield, "Covenants Implied in Registered and Unregistered Leases" in *Studies on the Law of Landlord and Tenant* at 75).

401 The Law Commission suggests that a revised set of implied statutory covenants should apply to all leases, registered and unregistered, including oral and statutory tenancies, and should entirely replace the common law and "usual" covenants - though, as at present, the parties could agree to exclude all or some of them. The legislation should distinguish between short-term leases (ie, those for one year or less) and long-term leases and should imply a full repairing covenant only in long-term leases, with a tenant under a short-term lease impliedly covenanting only to keep the premises in a "tenant-like condition". (We would welcome suggestions on how this last expression can be avoided, having struggled to find a short form of words to sum up the concept articulated by Denning LJ in *Warren* v *Kean* (para 396).)

402 Implied covenants may be something of a fall-back for people who have been unwise enough to proceed without any (or with incomplete) documentation. The range of implied covenants must be limited to those which would be appropriate *in any circumstance* as a means of filling in the gaps left by the parties. For this reason they are not particularly extensive or sophisticated. That must be left to persons drafting leases for particular circumstances and parties.

Rates and taxes

403 There is no covenant for the lessee to pay rates and taxes (on the part of the lessee) in section 106. The position of a tenant in relation to rates is usually expressly dealt with in a lease document. Where it is not, the position is governed by section 121 of the Rating Powers Act 1988 which makes an occupier of rateable property "primarily liable" to the local authority for rates becoming due and payable while his or her name appears in the rate records as the occupier of the property. "Occupier" is defined in section 2 of that Act as meaning the owner of the land "except where a person other than the owner has a right to occupy the land by virtue of a tenancy granted for a term of not less than 12 months certain, in which case the term "occupier" means that other person". When an occupier fails to pay rates the local authority can recover them from the owner or the first mortgagee (section 139).

404 There would appear, then, to be no need for an implied covenant concerning rates. (If the parties to a lease wish to vary the position they may do so by express covenant.) Similarly, the Land Tax Act 1976 (pending its repeal) and the Goods and Services Tax Act 1985 deal adequately with the question of liability for those taxes. There is no other relevant tax.

Quiet enjoyment and non-derogation

405 In the 1952 Act there are no implied covenants by the landlord for quiet enjoyment and non-derogation from the grant but, because they are not inconsistent with section 107, the common law covenants to this effect can be implied. We think that they should be expressly stated. The common law covenant for quiet enjoyment is in limited form; it protects the tenant only against interference by the landlord and a person who claims through the landlord but not against someone who has a superior title to the landlord. At present the Commission favours the adoption of an implied covenant in the limited form. Express covenants in absolute form are not commonly found. The Commission therefore is hesitant about recommending a statutory covenant which is significantly different from those adopted by conveyancers. Nevertheless, the limited covenant seems to have been a product of the pre-Torrens title system, when it was uncertain whether the lessor could make out the title in the event of challenge. That is no longer so in the vast majority of cases. There may therefore be a case for moving to absolute covenants for quiet enjoyment, as has been done in residential tenancies (section 38 of the Residential Tenancies Act 1986).

New implied covenants

406 Certain further implied covenants could be introduced, being (on the part of the lessee) covenants not to alter the premises without consent and not to cause nuisance or annoyance to the landlord or neighbours, and (on the part of the landlord) that the premises may be legally used for the purpose(s) stipulated in the lease. At present, the law may give the tenant no rights against the landlord if it transpires that the premises cannot be legally used for the purpose expressed in the lease, although a claim could be made under the Fair Trading Act 1986 if the landlord's conduct was deceptive or misleading.

Abatement of rent

407 Section 106(a) contains an implied covenant by the lessee to pay rent, but makes it subject to a proviso that the rent shall abate while the premises have been destroyed or damaged by fire and some other perils and have not been repaired. Many leases also expressly provide that upon destruction or substantial damage to the premises the term is to come to an end. We think that such a provision is inappropriate as a general implied term because of the widely varying types of premises and the difficulty of determining when there has been destruction or substantial damage in some cases (for example, a farming lease).

Repair of premises

408 We have already mentioned (para 91) the proposed distinction between short-term and long-term leases. Section 106(b) now requires the premises to be kept and yielded up in "good and tenantable repair, having regard to their condition at the commencement of the said lease" (subject to certain common exceptions). For a covenant of general application, in the absence of express agreement, it seems better to continue to limit the obligation of a tenant under a long-term lease to maintaining the premises as they were when the lease was granted. That condition may not be good. The question would be whether the premises have since deteriorated other than through reasonable wear and tear or one of the other exceptions. An obligation to keep premises in good condition may include an obligation to put them in good condition if they are not in that condition at the beginning of the term (*Payne* v *Haine* (1847) 16 M & W 541; 153 ER 1304). The requirement to have regard to the condition at the beginning of the term reduces the tenant's exposure to this rather unfair rule. Where a landlord wants premises to be improved by the tenant there should, we think, be express agreement to that effect. Perhaps the rule itself should be negated.

409 Section 106(b) also includes amongst the exceptions any "accidents". It does not seem appropriate to exempt accidental damage generally. At present it seems that "accidents" includes acts of the tenant and operations conducted in connection with the use of the premises except where the damage was intended or was the result of negligence. It must not have been of the kind which a reasonable person in the position of the tenant would have foreseen and could have guarded against (see *Saviane* v *Stauffer Chemical Co (Australia) Pty Ltd* [1974] 1 NSWLR 665 in which the New Zealand section is considered). But this is really most confusing. A more rational position, which would avoid the problems caused by the subrogation cases (for example, *Marlborough Properties Ltd* v *Marlborough Fibreglass Ltd* [1981] 1 NZLR 464 and *Leisure Centre Ltd* v *Babytown Ltd* [1984] 1 NZLR 318), would be to confine the exception to specified perils and exempt the tenant regardless of negligence. The landlord's insurance cover would extend to protect the landlord whether or not the tenant had been negligent. We return to this question in Chapter 15.

410 The list of risks to which the exemption would apply could read: "fire, flood or explosion (whether caused or contributed to by the lessee) or lightning, storm, earthquake, volcanic activity or any risk against which the lessor is insured". There would be no exemption for an insured risk if the lessee's act or omission vitiated the insurance cover.

Questions:

Q94 Should all common law and implied (usual) covenants be replaced by a new set of implied covenants in the Act?

Q95 **Should the new set of covenants be implied in oral and other informal leases (unless excluded by the parties)?**

Q96 **Is there any need for an implied covenant that the lessee pay rates and taxes?**

Q97 **Should there be implied covenants by the lessor for quiet enjoyment (in limited form?) and non-derogation from the grant?**

Q98 **Should a lessee under a lease for one year or less have any implied obligation to do more than keep the premises in a tenant-like condition?**

Q99 **Should a lessee who covenants merely to "repair" be obliged to put into repair premises which are out of repair at the commencement of the lease?**

Q100 **Is the proposed implied repair covenant (paras 408 and 409), which excludes liability for negligently causing fire and other events, suitable?**

LEASE COVENANTS RUNNING WITH AND AGAINST THE REVERSION

411 This is a topic of which it has been said that "the established rules ... are purely arbitrary, and the distinctions, for the most part, quite illogical" (*Grant* v *Edmondson* [1931] 1 Ch 1, 28, Romer LJ). And the language of sections 112 to 114 certainly does not make them accessible.

412 The proposals for reform which the Law Commission now puts forward in a preliminary way assume that any reference to a "covenant" in the proposed new Property Law Act will include promises made in informal leases, including statutes and oral tenancies. It is suggested that the rules of the new Act concerning the running of express or implied covenants should not differ depending on whether or not the lease and the estate out of which it is granted are legal interests, equitable interests or statutory or oral tenancies.

Privity of estate: common law rules

413 As between the original landlord and the original tenant, there is both privity of contract and privity of estate. In contract both remain liable for all of their covenants whether they relate to the land or are "personal".

414 Privity of estate exists between the parties to the lease only so long as the relationship of landlord and tenant continues. (It never, therefore, exists between a landlord and a subtenant and, of course, between those persons there is no privity of contract either.) When a lease is assigned, privity of contract continues but privity of estate ceases between the landlord and assignor. In the absence of a deed of covenant with the landlord by the assignee of the lease, there is no privity of contract between the assignee and the

landlord but there is privity of estate as soon as the assignee attorns tenant, which is usually done by going into possession and paying rent. The Law Commission puts forward the view that there should no longer be any need for attornment before privity of estate can exist between a landlord and an assignee: that it should arise automatically once an assignment takes effect - indeed, even before the landlord consents - but subject to the right of the landlord to withhold consent and treat the assignment as a breach of the lease where that is otherwise appropriate. (An assignment is effective before the landlord consents: see *Old Grovebury Manor Farm Ltd* v *W Seymour Plant Sales and Hire Ltd* (No 2) [1979] 1 WLR 1397.) The advantage for the lessor of automatic privity of estate is that it can pursue the assignee for a breach of the lease occurring after the assignment but before consent is given.

415 The Commission suggests that privity of estate should exist between landlord and assignee regardless of whether the assignment is of a registered or an unregistered lease and, in the former case, regardless of whether the assignment is by registered memorandum of transfer; nor should it be necessary for the assignee to have entered into possession. Our intention is to clarify the present uncertain position (see *Purchase* v *Lichfield Brewery Co* [1915] 1 KB 184, *De Luxe Confectionery Ltd* v *Waddington* [1958] NZLR 272 and R T Fenton "Assignment of Informal Leases" (1977) 7 NZULR 342). As we point out at para 281 this reform will affect the position of a mortgagee who takes an equitable assignment of a lease.

416 An assignee is liable for all covenants which relate to the land (the subject matter) and run with it - those which "touch and concern" the land - but is not liable for personal covenants.

417 Once the assignee completes a further assignment and so ceases to be the current tenant, then there is no longer any continuing liability to the landlord for subsequent events, unless it has been assumed by deed of covenant.

418 In contrast, when a landlord transferred the reversion the position at common law was that only the obligations inherent in the nature of the landlord and tenant relationship, such as the tenant's obligation to pay rent, were binding as between the transferee of the reversion and the tenant. The express covenants of the lease, insofar as they went beyond inherent obligations, did not bind either transferee of the reversion or tenant as against the other.

Existing statutory provisions

419 This disagreeable situation was remedied in 1540 by the Grantees of Reversions Act (32 Hen 8, c 34) which is in force in New Zealand (First Schedule, Imperial Laws Application Act 1988) and which, according to Megarry and Wade at 753, was enacted because of the seizure and distribution of monastic lands, it then being found inconvenient that the transferees

of the lands could not enforce existing leases. The statute is still in force in New Zealand but has, for practical purposes, been superseded, except in relation to easements and profits and leases granted before 1906, by sections 112 and 113 of the Property Law Act 1952. (Repeal of the 1540 Statute should be accompanied by a section in the proposed new Act replacing it in respect of easements, profits and other incorporeal hereditaments.)

420 Section 112 annexes to each part of the reversion all covenants of the lease "which relate to the subject matter of the land". This expression is a modern formulation of "touching and concerning the land" (*Hua Chiao Commercial Bank Limited* v *Chiaphua Industries Ltd* [1987] AC 99, 106-107 (PC)). The section, which must of course be read subject to the Land Transfer Act (para 16), gives the transferee of the reversion the right to enforce such covenants against the lessee (including a current assignee).

421 The distinction between purely personal covenants and those which touch and concern the land is one of the rules which can be criticised as being arbitrary and illogical. Most leases do not contain purely personal covenants. Where this is done it is easy enough for that fact to be spelled out. Indeed, it seems better for the question whether a covenant will run with the land to be determined by the intention of the parties (either express or implied), instead of by the somewhat arbitrary test of whether it relates to the subject matter. For example, if a tenant covenants to pay a sum of money, why should it matter, so far as the transmissibility of that promise is concerned, whether the payment is to be to the landlord or to a third party? If the landlord agrees to refund a bond, whether that obligation is to be assumed by a transferee of the reversion should depend upon the intention of the original landlord and the tenant who paid the bond. The determination of that intention will take into account such factors as whether the tenant, upon assigning the lease, was bound to assign the benefit of the landlord's promised refund. In reality the Privy Council in *Hua Chiao Commercial Bank Limited* v *Chiaphua Industries Ltd* in considering this point was engaged in determining the intentions of the original parties. That was the deciding factor which caused their Lordships to find that the obligation was personal and did not bind the transferee of the reversion. It may be better for the law to be reformulated in terms of this reality; for the test to be whether the covenant was intended to bind a successor, rather than whether it related to the land itself.

422 The Law Commission (England and Wales) in its report entitled *Landlord and Tenant Law: Privity of Contract And Estate* (Law Com No 174, 1988) has recommended that the distinction be done away with. PLERC in its *Final Report on Legislation Relating to Landlord and Tenant*, para 71, was more cautious, being concerned that a lease might in theory include provisions having nothing to do with the landlord and tenant relationship or that the lease could itself be incorporated as

part of a much more wide-ranging commercial relationship between the original parties. The Commission would be much helped by submissions on this point but at this stage does not share PLERC's concerns and favours the change suggested by the Commission in England.

423 One of the consequences of such a change would be that an option to purchase found in a lease would be enforceable against an assignee of the reversion. This seems consistent with section 118 of the Land Transfer Act 1952 which already permits registration of a lease containing such a clause.

424 Section 113, which in a sense is the converse of section 112, gives to the tenant (including any current assignee) the right to enforce against a transferee of the reversion, the covenants in the lease which relate to the subject matter. It is again suggested that the distinction could be done away with subject to any contrary intention expressed in the lease.

Covenants concerning future property

425 At common law a covenant did not run, except where it was expressed to be in favour of assigns, if it related to something which was not in existence when the covenant was made. This rule has already been abrogated in relation to leases by the final sentence of section 112(1) and in section 64. We see no reason why the abrogation should not be carried forward.

Leases granted before 1906

426 We have already noted at para 419 that the Grantees of Reversions Act 1540 remains in force in respect of easements and profits. Either a new section on this subject will need to be substituted for it, or sections 112 and 113 should be extended to cover easements and profits.

427 The 1540 Act is also in force in relation to leases executed before 1 January 1906 (the date of commencement of the Property Law Act 1905 when the predecessors of sections 112 and 113 first appeared in New Zealand legislation). Sections 112(6) and 113(2) limit those sections to leases made on or after that date. Prior to 1906 the position of an assignee of the reversion was governed by section 1 of the 1540 Act, it being the equivalent of section 112. It applied only to leases under seal (section 2 of the 1540 Act, equivalent to section 113, was not restricted in this way). Where a lease was granted before 1906 and was not under seal, a transferee of the reversion did not have the benefit of the lessee's covenants nor was the transferee bound by any of the lessor's covenants. (The lessee's obligation to pay rent or to do a service in the nature of rent is exceptional: it runs with the reversion at common law, independently of statute: see *Chapman v Moray Industries (1986) Ltd* (1991) 1 NZ ConvC 190,700.)

428 The requirement for the use of a seal by an individual in the making of a deed was dispensed with in New Zealand as long ago as the Conveyancing Ordinance 1842 (section 2) but the legislation in this country did not provide a consequential dispensation from the requirements of section 1 of the 1540 legislation.

429 With the passing of the years since 1905 it has become less and less likely that there are any remaining informal leases still in force and dating from before that time. Obviously any such informal lease, if it still is current, must have been for a term of more than 86 years. The Law Commission thinks it unlikely that any lease for such a long term would have been made in an informal manner, though it concedes the possibility that care may not have been taken in all instances to ensure that a deed of lease was sealed in a manner complying with the 1540 legislation.

430 The Grantees of Reversion Act 1540 assisted a person who acquired the reversion to enforce the lessee's covenants. Section 112 extends this assistance to anyone entitled to the income of the land. This was of particular importance in the case of a legal mortgage of deeds system land since the lessor/mortgagor ceased to be the reversioner because the legal estate was transferred to the mortgagee. But all land transfer mortgages operate as charges - and we consider that all mortgages of land should do so (para 270). For practical purposes the only person entitled to the income, to whom a lessee is now rendered liable by this extension of the Imperial legislation, is a purchaser of the reversion who has entered into possession but not yet taken title. There seems to be no good reason why such a person should not have the benefit of the lessee's covenants in a pre-1906 lease, for that is merely to bring forward an entitlement which will occur in due course when a memorandum of transfer is executed and delivered.

431 The Law Commission would like to recommend that in a new version of sections 112 and 113 there should be no exception for leases entered into before 1 January 1906 but before doing so is anxious to know whether there are current leases of that age which have been entered into without use of a seal.

432 In 1952 the legislature added to section 112(1) a stipulation that it was to extend to covenants to do an act relating to land, notwithstanding that the subject matter might not be in existence when the lease was made. It applied retrospectively to leases then current which had been executed after 1905. Probably it was thought that retrospectivity was unimportant in this instance because the common law appeared to have reached the same position (*In Re Robert Stephenson & Co Ltd* [1915] 1 Ch 802, 807). A further extension of this rule to pre-1905 leases can be made on the same basis.

433 The Commission also advocates that *personal* covenants should run with the lease and the reversion (para 421). There will certainly be some such covenants in leases current when a

new Property Law Act comes into force. In some instances the reversion may already have changed hands. Therefore, immediately before the proposed new Act commences there will be situations in which a lessee is not liable to the lessor, or vice versa, under a personal covenant contained in a lease. It would not be right that the new Act should impose liability under such a covenant which has already ceased by reason of a transfer of the reversion.

434 We have considered whether the benefit and burden of personal covenants which are still binding when the new Act commences should thereafter run with the reversion. We think that they should not. The burden of such a covenant on the reversion is likely to be expressly allowed for by the vendor and the purchaser of the reversion, but a lessee who is obligated under a personal covenant may have committed to it in the knowledge that its benefit was not transferable. We tentatively conclude that a new version of section 112 should extend to personal covenants only where they are contained in leases executed after the new Act comes into force.

Who may claim on covenant?

435 Until the decision of the majority of the English Court of Appeal in *Re King* [1963] Ch 459, as confirmed by the same Court in *London and County (A&D) Ltd* v *Wilfred Sportsman Ltd* [1971] Ch 764, there was doubt about whether the English equivalent of section 112 had the effect of transferring exclusively to a person who acquired the reversion the right to claim against the tenant for rent accruing due before the transfer or for breaches of covenant which had occurred before that time and were not continuing breaches. The Court has now confirmed that this is the case unless there is a contrary intention recorded between the landlord and the transferee. The English cases have been applied in New Zealand (*Paramoor Nine Ltd* v *Pacific Dunlop Holdings Ltd* (1990) ANZ ConvR 563). This position should be preserved.

Severance of reversion

436 Section 114 deals with the apportionment of rights and obligations of the parties where a reversion is divided amongst several landlords or the lease comes to an end in relation to part of the land only, continuing as to the balance. Technically these situations are respectively known as severance as regards the land and severance as regards the estate.

437 It is our present understanding that in modern New Zealand conveyancing practice a reversion would hardly ever be divided or a lease surrendered as to part of the premises without negotiation with the tenant and/or execution of an appropriate deed of variation and/or an agreement between the several reversioners. Section 114 refers to apportionment, without trying to spell out how this should occur. Perhaps that is wise, given the many possibilities. The common law already provides for appropriate division of rent amongst several reversioners; likewise performance of the tenant's

covenants is apportionable at common law. Given the rarity of the occurrence and the potentially large number of differing fact situations there would seem to be little advantage in trying to make the section more explicit, though its language is obscure and can certainly be modernised.

438 Section 140(2) of the Law of Property Act 1925 (UK) has a provision enabling a tenant who has received a notice to quit which operates as to part only of the premises, because there has been a severance of the land, to bring the entire lease to an end by notice to the landlord of the other portion of the reversion. This could be adopted.

Questions:

Q101 Should there be need for an act of attornment by an assignee of a lease before privity of estate exists between the assignee and the landlord?

Q102 Assuming a landlord retains the usual (rather limited) right to refuse consent and treat an assignment without consent as a breach, is there any reason why privity of estate should not exist whether or not there has been a consent?

Q103 Should an assignee remain liable to the landlord for breaches occurring after the assignee further assigns the lease, even though there has been no deed of covenant, ie, continuing liability is automatic once privity of estate has existed?

Q104 Should all covenants run with the lease and the reversion, not just those which "touch and concern" the land, unless the parties agree otherwise? If so, should this change in the law apply only to leases granted after the new Act commences?

Q105 Should leases granted before 1906 continue to be an exception to the usual rules relating to the running of covenants?

Q106 Is there any need to expand the present provisions of section 114 concerning severance?

IMPLIED COVENANTS UPON TRANSFER OR ASSIGNMENT OF LEASE

439 A person who assigns a lease has the benefit of an implied indemnity by the assignee against breaches committed by the assignee but when the assignee in turn transfers the lease, the implied indemnity from that assignee ceases and is replaced by an implied indemnity from the new owner of the lease (*Moule* v *Garrett* (1872) LR 7 Exch 101). Thus a lessee who assigns to a person of substantial worth accordingly enjoys the benefit of the indemnity from that person only so long as that person continues to be the tenant, and loses it, perhaps in favour of somebody with much lesser substance, once that person enters into a further assignment.

440 In contrast, section 98 of the Land Transfer Act provides for an implied indemnity by a transferee of a lease which does not lapse when the transferee disposes of the lease. It is suggested that this provision could well be lifted out of the Land Transfer Act and, with appropriate redrafting, put into the proposed new Property Law Act as a general provision relating to both registered and unregistered leases.

Question:

Q107 Should section 98 of the Land Transfer Act become a section of general application?

CONTINUING LIABILITY OF ASSIGNOR OF LEASE

Lease as contract

441 Lay people who sign a lease as tenant are often under the mistaken belief that their liability to the landlord will cease once they assign the lease with the consent of the landlord. They overlook the fact that a lease is a contract and that, as a general principle, one cannot rid oneself of liability under a contract merely by assigning it. Benefits are assignable, but liabilities are not.

442 Under the present law a tenant who assigns a lease remains contractually bound to perform all tenant's covenants contained in the lease for the balance of the term and for the period of any extension of term or renewal of term to which a right is given in the original lease. (In relation to extensions or renewals see, however, dicta of the Court of Appeal in *W E Wagener Ltd* v *Photo Engravers Ltd* [1984] 1 NZLR 412 which suggest that liability does not continue when there has been a new grant. But is this correct? Every extension or renewal requires a new grant.) The length of the potential exposure of the assignor may be of many years' duration. During that time the tenant often loses touch with the premises, may have no knowledge of the identity of the current tenant, since there may have been intermediate assignments, and will have no control over the situation. If the landlord chooses to pursue the original tenant, the latter has the right to be indemnified by the current tenant, but usually the landlord pursues the original tenant only because the current tenant has become insolvent. In these circumstances the original tenant's rights against any intermediate tenant will depend upon the existence of a chain of deeds of indemnity.

Concurrent liability

443 The problem is even worse. An assignor has concurrent liability with the current tenant. The assignor is *not* a guarantor of the liability of the current tenant and consequently is not released, as a guarantor would be, by dealings between the landlord and the current tenant to which the assignor has not consented.

444 By assigning the lease the assignor impliedly authorises the assignee (and any successor of the assignee) and the landlord to do in relation to the lease whatever the assignor could have done (*Centrovincial Estates plc* v *Bulk Storage Ltd* (1983) 46 P & CR 393). That includes entering into variations of the lease.

445 Some "variations" may not be objectionable. The exercise by the landlord of a right to review the rent and the exercise by the assignee of a right of renewal, upon which the rent is also adjusted, are matters contemplated by the lease, which the assignor should have had in mind when deciding to transfer the leasehold estate to the assignee. In other words, when choosing the assignee and seeking the landlord's permission to assign, the assignor should have taken into account the continuing liability and also the fact that the liability might be increased upon a rent review or by reason of the exercise of a right of renewal contained in the lease. It seems to the Commission that a guarantor would not be released by such matters because they would not be seen as true variations. Nevertheless, if the law is changed so as to make an assignor a guarantor rather than a concurrent obligor, it would have to be made clear that the assignor's liability was not released by the fixing of the new rent in these circumstances by agreement reached in good faith between the landlord and the assignee or, in the event of disagreement, by valuation or arbitration. It is impracticable to require the landlord to obtain the assignor's agreement to rent reviews.

446 However, the liability of an assignor for true variations (for example, an agreement by the landlord to spend money improving the premises in return for a promise by the assignee to pay a higher rental) is most unusual and is not something which a lay assignor should be expected to anticipate. A guarantor would usually be released. The unfairness of continuing liability of this uncommon nature over a long period seems very clear.

English Law Reform proposal

447 The Law Commission of England and Wales in its report entitled *Landlord and Tenant Law: Privity of Contract and Estate* (Law Com No 174 1988) has proposed radical change. In essence, that Commission suggests that after an assignment the assignor should be released but that the landlord should be empowered to insist that the assignor guarantee the performance of the immediate assignee. Even that guarantee would lapse when the assignee ceased to be the tenant so that, on a second assignment, the landlord would lose the personal covenant of the original tenant/assignor. This report has not yet been implemented by the legislature.

New Zealand statutes

448 In New Zealand, in the case of a residential tenancy, section 44(6) of the Residential Tenancies Act 1986 provides that, upon an assignment by a tenant with the consent of the landlord and in accordance with any conditions attached to

that consent by the landlord, the tenant ceases to be responsible to the landlord for the obligations imposed upon the tenant by the agreement and by the Act (but without prejudice to any liability already incurred by the tenant to the landlord in respect of anything done or omitted to be done before that date). Section 64A of the Property Law Act dealing with positive and negative covenants running with the land is to similar effect. The covenants become binding when the land is acquired and cease to be binding when it is disposed of, the incoming purchaser taking over the liability at the same time as the benefit.

PLERC report

449 In contrast, in its *Final Report on Legislation Relating to Landlord and Tenant* (1986) PLERC, in paras 73-75, came to the conclusion that, in relation to non-residential tenancies, tenants should remain liable after assignment of their interests if they were the original party to the lease or had executed the usual deed of covenant with the landlord. It seemed to that Committee that the present law provided some balance between the rights of the landlord and the rights of the tenant. It is usually not very difficult for a tenant who wishes to assign a lease to compel the landlord to consent. The landlord who objects has to show that the proposed assignee is unsuitable. On the other hand, the landlord, although forced to accept a tenant who might not have been chosen in the first place, receives some protection because of the ongoing obligation of the assignor. The Committee commented:

> Viewed in that context the existence of the on-going obligation might not be unfair. In practice, if an assignee is going to default on the payment of rent it more often than not happens fairly soon after the assignment. Not many assignors are troubled by a claim from the landlord years after the assignment has taken place. The Committee believes that, were the law to be changed so that an assignor was released from contingent liability once the assignment was completed, it might become much easier to persuade a court that a landlord should not be obliged to consent to a proposed assignment. It would not be in the interests of tenants if the current lenient attitude of the courts were to change in this way.

Problems with English proposal

450 If the English proposal were to be implemented, the original tenant turning into a guarantor, but of the immediate assignee only, several unfortunate developments might emerge. The courts might more readily uphold objections by the landlord to the assignment by the original tenant. Or the courts might uphold the landlord's objection to the further assignment of the lease by the assignee (since that assignment would have the effect of releasing the original tenant from the guarantee); in this way the assignee might become locked

into the lease until able to produce a further assignee of financial strength equal to that of the original tenant. If the courts do not assist a landlord in this way the advantage of a strong personal covenant from the original tenant would be lost by a series of assignments. Indeed, the cunning tenant who wished to escape from the lease might be able to engineer them. This aspect of the problem is not canvassed in the English report. It seems to us that tenants might prefer to retain their existing "easy" right to assign and be at once relieved from the obligation to pay rent, even if that involves continuation of a relatively remote contingent liability.

451 The Law Commission presently favours the middle ground and tentatively suggests that the law might be reformulated as follows:

- After an assignment a tenant would continue to be liable to the landlord for the performance of the assignee and successors in title to the assignee, but the tenant's liability would be that of a guarantor rather than of a concurrent obligor. (This would also be the position of an assignee who in turn assigned the lease since, under our proposal, each assignee becomes automatically bound by all covenants (para 415).)

- The assignor would be liable for rent increases under a review clause and would be liable during the period of any renewal provided for in the original lease. This would include liability for an increase in rental on the exercise of a right of renewal or under a rent review provision operating during the renewed term.

- Contracting out would not be permitted, for otherwise every landlord might in practice insist that the tenant assumed concurrent liability as at present.

- If the landlord sold part of the land comprised in the lease so that more than one person became landlord under the same lease but in respect of separate parts of the property (an unusual situation in New Zealand conveyancing), a variation made between an assignee and one of those landlords would release the assignor of the lease as to that portion of the property only.

452 We have considered and rejected the idea that the assignor should be released merely by the lapse of time (eg, two years from the date of the assignment). We can see no logical basis for this. It would involve an arbitrary interference with the lease contract, unrelated to the length of the term. We would have difficulty in fixing a cut-off point, unless it were to be very distant from the assignment. Even then it would have to be chosen in an arbitrary way.

453 A further possibility is to empower an assignor to apply to the court for an order releasing the assignor from ongoing liability under the lease either in whole or in part. Presumably a court would exercise such a discretion sparingly: in circumstances where the personal covenant of the current tenant (or anyone else bound to the landlord under the lease) was very strong. We are less persuaded about this proposal because the experience of the commercial community over the last few years suggests that the court might be very reluctant to exercise such a power and consequently the section might be a dead letter. We explore the possibility because of the difficulty that can be caused to trading companies who are bound by an ongoing contingent liability of nominally large amount, which cannot be completely disregarded even though it is not very likely to become an actual liability.

454 This subject raises issues which are as knotty as any considered in this preliminary paper. The Law Commission does not pretend to have found a satisfactory answer and would be most grateful for comments and suggestions on the plight of the assignor.

Questions:

Q108 **Should any, and if so what, change be made in the current law concerning liability of an assignor of a lease?**

Q109 **Should a tenant be released upon assigning the lease (with the landlord's consent) and the landlord prohibited from requiring a guarantee from the assignor except only of the immediate assignee's performance?**

Q110 **Alternatively, should the law be changed as suggested in para 451?**

Q111 **Would the power to apply to the court as in para 453 be of practical value?**

XIV
LESSEE'S LIABILITY FOR NEGLIGENTLY DAMAGING PREMISES

EFFECT OF STANDARD EXCLUSION OF RISKS

455 Most leases contain a provision excusing the tenant from liability to repair or reinstate the premises in circumstances in which they have been damaged by fire or some other peril. The implied covenant found in section 106(b) that the tenant will keep the premises in good and tenantable repair having regard to their condition at the commencement of the lease contains an exclusion for "damage from fire, flood, lightning, storm, tempest, earthquake ... all without neglect or default of the lessee" excepted. We are proposing to carry this provision forward (see paras 408 to 410) but in a different form which will, we hope, be consistent with the proposals set out in this chapter.

456 However, it is established that even if an exclusion simply refers to the excepted perils and makes no mention of the tenant's neglect or default, when the tenant has in fact caused the peril by its negligence, the landlord will not be prevented by the exception clause from succeeding in a claim against the tenant based on that negligence. In other words, it makes no difference whether or not the exception clause expressly excludes negligence from the exception (*Marlborough Properties Ltd* v *Marlborough Fibreglass Ltd* [1981] 1 NZLR 464 (CA)).

457 When a property owner takes out insurance on its property it seeks the protection of the cover against all forms of destruction or damage caused by an event coming within the description in the policy. The property owner does not for this purpose distinguish between negligent and non-negligent acts; nor does the policy. If the property burns down the owner expects to receive the insurance money even though the fire may have been caused by the negligence of the owner. Where properties are tenanted, owners would correctly assume that they will be protected under their insurance policies against perils caused by the negligence of their tenants. They may also assume that tenants too have the benefit of the cover. It is certainly the experience of those whom we have consulted that most tenants believe that they are protected under insurance cover arranged by their landlords. It does not usually cross their minds that, if their negligence is the cause of the destruction of the premises, they may be liable for it in an action brought by the landlord or the insurer of the landlord.

458 However, the legal position is otherwise. A tenant is, in the absence of agreement to the contrary, legally responsible to the landlord for its own negligence and that of its agents which results in damage to the property. Any limitation to that exposure depends upon the lease documentation: in particular, upon the covenants concerning payment of rent and insurance premiums, repair and destruction

or damage to the premises. Caselaw and our own inquiries show such lease covenants come in a variety of forms, many of which are difficult to comprehend without an understanding of the common law, including a reading of the often complicated cases themselves. Many of the distinctions made in the lease covenants have been interpreted by the courts in a way which gives them a subtlety which might be thought to have been unintended by the draftsperson.

The economic reality

459 The underlying economic reality is that the landlord has a property which it wishes to insure. To do so it needs money to pay the premiums. The source of that money will be the rent to be received from the tenant. In some cases this connection is plainly spelt out: the landlord covenants to insure and the tenant to pay or reimburse the premium. At the other extreme there may be no covenant to insure and nothing said about payment of premiums. But, if the landlord voluntarily insures, the cost of doing so will certainly be a factor in the bargain struck over rental. Even if the landlord does not mention it to the prospective tenant, the landlord will be aware of and take into account its costs in connection with the building when bargaining for rent. In this sense the rent can fairly be regarded as the means by which the landlord procures the protection of insurance. And we repeat that the landlord seeks the insurance cover in respect of negligent acts as well as those where no element of negligence is present.

CASELAW

460 Surprisingly, the caselaw in Commonwealth jurisdictions does not reflect this position but proceeds instead upon a scrutiny of individual lease contracts, arriving at conclusions which may be thought to be at odds with reality and to turn on fine, and probably unintended, nuances in the wording. The cases are not easy to reconcile. It is also noteworthy that appellate courts in New Zealand and Canada have had difficulty in reaching their conclusions: there are some strong dissenting judgments.

461 We mention some of the cases by way of example. In *Ross Southward Tire Ltd* v *Pyrotech Products Ltd* (1975) 57 DLR (3d) 248 and *Mark Rowlands Ltd* v *Berni Inns Ltd* [1986] QB 211 the landlords covenanted to keep the premises insured and the tenants to meet the premiums (or, in the latter case, a proportionate part corresponding with the proportion of the building which was comprised in the premises). But the policies were in the sole names of the landlords. However, the court in each case was able to reach a result which, in effect, meant that the insurance was for the benefit of the tenant as well as the landlord, holding that the tenant was not obliged to reimburse the landlord for the loss caused in a fire where the tenant had been negligent. The landlord's loss by reason of the tenant's negligence was to be recouped from the insurance moneys and not passed on to the tenant.

462 In New Zealand in *Marlborough Properties Ltd* v *Marlborough Fibreglass Ltd* (see para 456) the lease provided for the tenant to insure the premises in the name of the landlord and to meet the premiums. The Court of Appeal (but only by a majority) found that the object of the insurance cover was to protect the landlord against the risk, whether it was accidental or caused by negligence, including negligence of the tenant. The exemption in the tenant's repair obligation relating to fire was only for fire caused "without neglect or default of the lessee" but the majority of the Court did not regard this factor as militating against the conclusion which they had arrived at for, if the words in question had been omitted from the repair clause, the tenant would still have been prima facie liable in negligence under the clause. The Court read the words in their context as extending only to such damage as was not covered by the insurance provided for elsewhere in the lease document.

463 Other tenants have not been so lucky. In a later decision of the Court of Appeal, *Leisure Centre Ltd* v *Babytown Ltd* [1984] 1 NZLR 318, the landlord covenanted to take out insurance cover and to apply insurance moneys in reinstating and making good any damage but the tenant was not required to pay or reimburse insurance premiums separately from the rent. The Court found that the tenant was not exonerated from liability for negligence because, it said, there was a reasonable and expressed "commercial" explanation for the insurance provision, namely that the landlord had covenanted to reinstate damage falling short of destruction of the premises and that insurance would provide a fund to enable repair and reinstatement of the premises for the benefit of both landlord and tenant in that circumstance. The reinstatement clause in that case also benefitted the tenant, it was said, by providing for abatement of rent until the damage was made good regardless of the cause of the fire. (But although the rent abated, the tenant was found to be liable for the cost of repair.) The tenant contended that the reasonable implication was that the clause was intended to protect both parties against all risks covered by the insurance policy. However, the Court found that the lease did not say so: it was not enough that the implication suggested by the tenant was reasonable from the terms of the lease or that the express provisions were capable of supporting such an implication. The test was necessity: whether the terms of the lease *required* the implication. Since another explanation could be found which did not absolve the tenant, the Court found that the landlord (or its insurer pursuant to its right of subrogation) could recover the cost of repairing the fire damage to the premises.

464 In *Perimeter Investments Ltd* v *Ashton Scholastic Ltd* [1989] 2 NZLR 353 the lease did not place on the landlord any obligation to insure but said that, if the landlord did so, the tenant was obliged to reimburse the premiums. In this case also the tenant was held liable for a fire caused by the negligence of one of its employees. The tenant's payment of

the premium was found to be explicable both as a means whereby the landlord could ensure itself of a net return and as a source of a fund to meet the cost of reinstatement, which could be of benefit to the tenant.

465 As we have indicated above, the Law Commission finds these distinctions very artificial. We do not believe they are seen as being "commercial". They appear to assume that when leases are negotiated the implications of rental, repair and destruction and damage clauses are carefully and knowledgeably considered. The experience of legal practitioners whom we have consulted suggests otherwise.

RESIDENTIAL TENANCIES

466 The Residential Tenancies Act 1986 does not grapple with the problem. Section 40(2)(a) requires that the tenant shall not "carelessly damage, or permit any other person to damages, the premises". Tenants are responsible for the actions of their licencees (section 41). Section 59 provides that on destruction of, or serious damage to, the premises, either party can terminate the tenancy by notice to the other. The Act is silent on the question of insurance. Any reform should therefore extend to residential tenancies.

PROPOSAL

467 The Law Commission has considered whether it would be better law if, where a landlord is able to obtain reinstatement or indemnity from its own insurer, it were not then able to claim against the tenant by reason of the tenant's negligence. In such a case the claim would usually be instigated by the insurer of the landlord. Therefore such a provision in the proposed new Property Law Act would have the effect of nullifying the insurer's right of subrogation. There would be no right in the landlord to which the insurer could be subrogated.

468 It seems to us that such a change in the law involves a consideration of several questions:

- whether it is reasonable to place on the landlord the risk of inadequacy in the amount of its insurance cover (an uninsured landlord would be able to claim but *any* amount of cover against the particular peril causing damage to the premises would preclude a claim against the tenant);

- whether in assessing risks in relation to a tenanted building the insurance industry treats the existence of a right of subrogation against the tenant as being material;

- whether such a change in the law is likely to lead to any increase in the level of premiums and, if so, whether that increase would be a burden, no doubt passed on to tenants,

> disproportionately great as compared with the benefit of the new rule.

Who should bear risk?

469 In relation to the first question, namely whether the risk of inadequate cover should be on the landlord, we have formed the tentative view that it should. Except in the minority of situations where the lease arrangement requires the tenant to arrange cover (which is not, we would have thought, an advisable stipulation for a landlord to make), it is the landlord who has control over the situation. The landlord has the greater interest to be protected and can make an informed decision concerning the level of cover. It will usually be able to arrange cover which is both comprehensive and full, often on a reinstatement basis. It can also make arrangements with the insurer so that cover is not cancelled or modified without adequate warning. If some unusual factor prevents or makes uneconomic the obtaining of full cover, the landlord is in a position to negotiate lease terms which apportion the risk between the parties.

470 A tenant can protect itself against exposure because the landlord is totally uninsured by stipulating that the landlord insure in some degree against specified risks, such as fire, flood and explosion, which are the commonest of the perils.

Subrogation: the position of landlord's insurer

471 The proposal here being considered is not new in New Zealand. It was discussed by the Contracts and Commercial Law Reform Committee in the mid-1980s shortly before that Committee went out of existence. Its cessation prevented any final conclusion being reached on the subject on that occasion. However, submissions were made by interested parties, among them the Insurance Council of New Zealand Inc who commented on the attitude of the insurance industry to the right of subrogation as between lessor and lessee. The Committee had pointed out that the present law might require a tenant for its protection to obtain and pay for its own separate insurance cover. Thus, in a sense, the premises might be insured twice, though for differing interests and differing risks.

472 We quote the response of the Insurance Council:

> The right of subrogation is an important one to the insurance industry. Upon the existence of that right rests much insurance industry practice as to the assessment of risk and the setting of rates. The Council notes with concern the views set forth in ... the discussion paper and suggests, with respect, that those views are based upon faulty reasoning and to an extent an emotional view of the insurance relationship on the part of the author of the paper....First, the author assumes that in the circumstances set forth in the paper the tenant is paying an insurance premium

twice. A more sensible and factual assumption is that the existence of the right of subrogation is taken into account in setting the rate and a change in the law will accordingly increase the risk to the insurer. The result of the proposed change will therefore be to increase premiums.

A second underlying assumption is that where an insurance contract exists it should exist for the benefit of all those who have an interest in the subject matter of that contract, no matter whether they have paid a premium nor how remote their interest. That course of reasoning flows from the statement "it seems wrong that a tenant should have to arrange his own cover to properly protect himself." The contract of insurance is a contract of indemnity designed to indemnify the party seeking indemnity in respect of risks which he incurs. The insurer, to quote the classic phrase so often used, "stands in the shoes" of the insured, and for valuable consideration assumes his risks and his remedies. The credibility of the contract depends in part on the ability to assume both the risk and the remedy. It is open to a tenant to indemnify himself against his own risk. Like his landlord, he has access to the insurance mechanism.

The insurance industry has felt constrained to comment in the past that much pressure for so-called insurance law reform stems from the result of poor commercial practice or understanding of the law, frequently on the part of the legal profession. If leases are properly drawn and perused, and clients adequately advised with regard to the insurance implications of their contracts by their advisers, then no practical difficulty arises. To say that it is highly unsatisfactory that a tenant's liability should turn on the chance way in which a provision in a lease has been formulated begs the question entirely. The formulation of a provision in a lease should not be a matter of chance. The law is clear and the availability of the insurance mechanism to provide indemnity quite obvious. The essence of the proposal is that a remedy should be removed from an indemnifier to protect a tenant who or whose advisers have been lazy or inept. The answer to the question posed ... must clearly therefore be that a lessor's insurer's rights of subrogation should never be taken away except where the lessor and insurer agree.

473 The Law Commission thinks that this puts the industry's case well but, with respect to the Council, it is unconvincing. It is all very well to point to the fact that landlords and tenants should be properly advised and to complain that often the advice is less than adequate. That is

no doubt so. But the fact remains that the law is, as we see it, out of kilter with the expectation of lay tenants and that they may, even once it is properly explained to them, be faced with a landlord who is unwilling to agree to protective terms. For example, the landlord may be unwilling to agree to the naming of the tenant in its insurance policy as a co-insured. The tenant, then seeing an exposure for negligence, is obliged either to run the risk or to pay for additional cover. That might not in itself be burdensome if, as the Insurance Council contends, the levels of premium respectively charged to the landlord and the tenant truly reflect the existence of the right of subrogation, ie, the landlord's premium is lower because the insurer will be able to recover from the tenant (or its insurer) in the event of a loss caused by tenant negligence and the tenant's premium is calculated on the basis that the risk is solely the tenant's negligence.

Is subrogation relied upon?

474 There is no evidence, other than the bare assertions of the industry, that the existence of a right of subrogation is in fact taken into account in the fixing of premiums. The industry's interest in subrogation would appear to be almost entirely *ex post facto*: when a fire occurs the landlord's insurer is at that point interested in exercising the right of subrogation. Recovery by means of it would seem to be a bonus which is not taken into account when the insurance cover is arranged and the premium struck. We make these comments after a consideration of industry practices based on the experience of those whom we have consulted and upon discussions with members of the industry.

475 We note also the judgment of Hardie Boys J in *Guthrie House Ltd* v *Cornhill Insurance Co Ltd* (1982) 2 ANZ Insurance Cases ¶60-466. In that case the defendant insurer had refused to meet the insured lessor's fire insurance claim on the basis that the lessor had failed to disclose a material particular, namely, a provision in the lease whereby the plaintiff, as lessor, had bound itself to require the lessee to reinstate fire damage only where the fire arose from the lessee's default *and* the default was such as to vitiate the lessor's insurance policy. (So that, in the only circumstances in which the insurer could be called on to meet a claim under the policy, it would have no claim by right of subrogation against the lessee even if the fire were the lessee's fault.) In other words, the lease, like the Auckland District Law Society's standard commercial lease form to which we will refer (para 481), created between landlord and tenant a situation of the kind contemplated by the proposal which we are considering.

476 The insurer complained that although it was told in the proposal that the building was to be tenanted, it had not been told that the lease limited the lessor's rights, and, in consequence, the insurer's rights by subrogation against the

lessee. (We pause to note that our proposal - paras 482 to 485 - would not prevent an insurer from stipulating that cover might be withdrawn if premises are leased or if lease documentation is unsatisfactory to the insurer.) Hardie Boys J had to consider whether the existence of the provision in the lease which exonerated the lessee from negligence was material in an objective sense: whether knowledge of the fact would affect the mind of a prudent insurer in its decision whether to accept the risk or what premium to charge. It had to be a fact which in the mind of a prudent insurer would affect the risk in one or both of those two respects.

477 Evidence was called by both parties from persons with extensive experience in the insurance industry. A witness for the insurance company said that although he would expect the lessor to make a copy of the lease available to the insurer, insurers did not as a matter of general practice concern themselves with the detailed provisions of leases. To the extent that they did so, their interest would be mainly directed to ascertaining for the purposes of their particular client where the responsibility lay, as between lessor and lessee, for the various types of insurance that might be required. He also said that the absence of rights of subrogation was material to the risk. The manager of the insurance company also confirmed that, as an underwriter, he would be loath to issue cover in the absence of a right of subrogation. The Judge, however, treated this with some reservation.

478 An expert called by the plaintiff landlord stated that the only interest shown by insurers in leases was to establish who was responsible for arranging the necessary types of cover. He said that it was quite common for leases to absolve lessees from liability for fire damage to a greater or lesser extent and that this was a fact well known to underwriters but of no significance to them either in the acceptance of the risk or in the rate of premium to be charged. He pointed out the various and different functions which are performed by different departments of an insurance company. We quote the manner in which this evidence is recorded in the judgment:

> One, whose function is to obtain or retain business, does not, he said, take cognizance of rights of subrogation in determining whether to issue cover and if so the rate of premium to be charged. Another, the claims department, upon having to meet a claim naturally enough looks carefully to see what rights it is able to exercise by subrogation, and whether it should seek to exercise them. These two functions, he said, are quite distinct. Subrogation is of concern in the latter, not in the former. (at 77,608)

479 The Judge referred to *Tate* v *Hyslop* (1885) 15 QBD 368 and endorsed a statement by Brett MR (at 375) as according with the present-day experience described by the witness.

Brett MR had said that an underwriter's right to salvage (by subrogation) was not a material fact. It would have been immaterial to the risk and immaterial to the insurance. In that case the right of subrogation had been restricted by contract. That restriction was said to affect neither the physical nor moral hazard. Hardie Boys J summed up the position:

> Thus I think that so far as subrogation is concerned, the insurer takes his client as he finds him. Whether or not there will be rights of recovery against a third party in the event of loss is not material to the assumption of the risk. It is certainly material in other respects. In general administrative planning, and in general actuarial calculations, the overall relationship of recoveries to claims met will be of great importance. But that is a different matter altogether. (at 77,610)

PRESENT POSITION

480 Nothing has emerged from our inquiries to suggest that the position of insurers has changed since this decision was handed down in 1982. One of our consultants, Mr John Marshall of Auckland, who has studied this subject for many years, comments:

> From discussions with the insurance industry the following statements can be made:
>
> (a) Occupancy of a building by a tenant as distinct from the building owner will not attract payment of a higher insurance premium. The rate of premium payable is assessed having regard to the nature of the business use and not to the identity of the occupier.
>
> (b) The insurance industry does at times concern itself with the identity of the occupier particularly in cases where certain persons are an identifiable insurance risk. At large, however, the industry does not inquire as to who are the tenants of buildings insured.
>
> (c) Insurance companies will usually note a tenant's interest on request and such noting will not attract payment of any increase in the insurance premium otherwise payable.
>
> (d) Insurance companies do not, except in special circumstances, concern themselves as to the covenants contained in a tenant's lease.
>
> The reality of the situation is that the insurance industry is happy to insure buildings throughout New Zealand without any concern as to who are the

> tenants or the terms of the lease, the industry's sole concern being with the nature of the business usage so as to fix the appropriate rate of premium. In these circumstances it is submitted that there is no valid reason why the benefit of the insurance cover should not be automatically conferred on tenants.

This seems fairly to sum up the position. The industry does not rely upon subrogation and does not discount premiums depending upon whether or not it is effectively taken away by lease terms.

A COMMONLY USED LEASE FORM

481 The standard form of commercial lease developed by the Auckland District Law Society contains lease covenants providing:

- that the tenant is not liable to make good fire damage where the landlord is insured against the risk of fire damage; and

- for an indemnity clause whereunder the tenant is liable to indemnify the landlord against loss or damage, but with a proviso to the clause that the tenant is not liable to indemnify where the landlord is indemnified under any policy of insurance.

It has been noted by some solicitors and brokers that these clauses nullify the right of subrogation of the landlord's insurer but it does not appear that landlords using the form have encountered difficulty in arranging cover or been asked to pay higher premiums.

SUGGESTED REFORM

482 We tentatively propose that the new Property Law Act should contain a section providing that where leased premises are destroyed or damaged by fire, flood or any other peril against which the lessor is insured or has covenanted with the lessee to insure, the lessor shall not be entitled to require the lessee to make good the destruction or damage or to indemnify the lessor in respect of the destruction or damage or to pay damages in respect of it. If, in these circumstances, the lessee is obliged by the terms of the lease to carry out remedial works, then the lessor would be obliged to reimburse the cost of so doing. It would be spelled out that the provision would apply regardless of whether the destruction or damage has been caused or contributed to by the neglect or default of the lessee. It would also be stated that the section would not excuse the lessee from liability for wilful damage. The section would not apply if the insurance moneys were rendered irrecoverable by the act or default of the lessee or the lessee's agent, contractor or invitee.

483 We have also considered whether any such provision should be mandatory. If it was not, there would be the danger that courts would continue to construe lease covenants in an artificial manner, as we believe that they have done in some of the cases to date, and might hold that by implication the parties had agreed to override the section. In such circumstances the suggested new implied repair covenant (paras 408 to 410) would, of course, have been excluded.

484 The argument against making the new provision mandatory would be that it would prevent an insurer from insisting upon exclusion of the new rule which we propose. However, the evidence which we have seen so far suggests to us that where insurers have a real concern at the time when the insurance contract is entered into, that concern is directed more to the nature of the tenant's user. Nothing in the Law Commission's proposed section, if it were mandatory, would prevent an insurer from requiring payment of a higher premium reflecting the greater risk and the fact that a claim would not be able to be made against the tenant if its negligence caused loss. For its part the landlord could require the tenant to meet the extra premium and could stipulate that, if insurance cover were withdrawn, the lease should be terminated. And, obviously, if this situation were unacceptable to the insurer it could decline to give or continue the cover. The Law Commission therefore favours making the provision mandatory.

485 We consider that the proposed rule should protect the tenant in relation to the whole of any building in which the premises are situated as well as in relation to the premises themselves. Such an extension will avoid a trap for tenants who might easily overlook the possibility of causing negligent damage to another portion of the landlord's property.

Questions:

Q112 **Should an insured landlord or its insurer be able to claim against the tenant for damage to the premises caused or contributed to by the tenant's negligence?**

Q113 **Should the risk of *inadequate* insurance cover (other than when vitiated by the tenant) fall on the landlord?**

Q114 **Who should bear the risk if there is *no* cover?**

Q115 **Should any new rule be mandatory?**

XV
SUBLEASES

SUBLEASE FOR THE SAME OR LONGER TERM THAN THE HEAD LEASE

486 Sometimes, often simply because of a mistake, a person holding land under a lease for a fixed term purports to grant a sublease for a term expressed to expire at the same time as that lease or even at a later date. Clearly in these circumstances the grant cannot take effect as an interest in land in respect of the period after the end of the term of the head lease, though it will enable the grantee to claim damages for any loss suffered if the grantee is unable to enjoy possession of the premises after the head lease has terminated.

487 But the consequences of a grant of this kind may be rather more unexpected, at least for lay persons. To operate as a sublease a grant made by a lessee must be for a term expiring earlier than the expiry of the head lease, because otherwise the grantor will be left with no reversion in the land. In the absence of a reversion there can be no relationship of landlord and tenant between the grantor and the grantee because a lease can only be granted out of a reversion.

488 A grant for the same or a longer term than the term of the head lease operates as an assignment of the head lease to the so-called sublessee, with the result that privity of estate then exists between that person and the landlord for the balance of the term of the head lease. The grantor is deprived of any remaining interest in the land. The relationship between the parties to the "sublease" is that of vendor and purchaser of the head lease. For recent New Zealand authorities on the nature of the relationship which arises see *Olympic Corporation Ltd* v *Orcatory Road Properties Ltd* [1990] 2 NZLR 519 (CA); *Neva Holdings Ltd* v *Wilson*, unreported, Court of Appeal, 26 April 1991, CA 66/90 and *Robert Jones Investments Ltd* v *W F & E L King Ltd* (1990) ANZ ConvR 539.

489 In determining whether the grantor has divested the entire interest in the premises, so that there is no remaining reversion, the court looks at the final expiry date of the head lease on the assumption that all renewal rights or rights of extension available to the sublessor will be exercised. This must be assumed because the sublessor is contractually bound to "keep the head lease alive". But the Court of Appeal in *Neva Holdings Ltd* v *Wilson* said that it should not be assumed that the sublessee will necessarily renew the term of the sublease. In that case the head lease was for four years from 1 March 1984 with three rights of renewal for four years each, ie, till 28 February 2000. The tenant granted a sublease until 1 March 1992 with a right of renewal till 28 February 2000. Because there was no certainty that the sublessee's right of renewal would be exercised - and therefore a reversion might remain in the sublessor - the arrangement was held to be a sublease rather than an

assignment. But in another case there was held to be an assignment where the sublease was for a term expiring before the termination date of the head lease but with a proviso that the sublease would continue quarterly until one of the parties gave three months' notice. Any such notice could not expire until after the termination date of the head lease (*Milmo* v *Carreras* [1946] 1 KB 306).

490 When a lessee with a right of renewal wishes to sublease beyond the term of the existing lease and into the renewal period, the parties may provide for the sublease to terminate one day before the head lease and to be renewed when the head lease is renewed. Alternatively, the lessee may agree to hold the premises in trust for the sublessee on the last day of the term, pending the renewal, as was done in *Robert Jones Investments Ltd* v *W F & E L King Ltd.* Both precautions seem unnecessary provided the sublessor does not make a grant which will equal or exceed the renewal period(s) which are available to it. But in either case the sublease would terminate if the sublessor neglected to renew the head lease.

491 The law on this subject was reviewed by PLERC in its *Final Report on Legislation Relating to Landlord and Tenant* (1986) at paras 84-85. The Committee pointed out the unexpected consequence that the operation of the sublease as an assignment created privity of estate between the sublessee and the head lessor rendering the sublessee liable to pay rent and other moneys due under the head lease, without benefit of any deduction. They also pointed out how convenient it would be, where the head lease is renewable and the sublease purports to extend into part of the renewal period, if the intended sublessee could be treated as a sublessee for the whole of the original term and the appropriate part of the renewal term.

492 The Committee recommended the abolition of this technical rule of law, so as to give effect to the intention of the parties:

> Provision could be made that the mere fact that a purported sublease extends to the end of the term of the head lease or more, should not of itself constitute the sublease an assignment, in the absence of other indications that that is to be the intended effect of the arrangement. (para 85)

They noted that questions of liability between sublessor and sublessee might arise where the sublease was granted for a term beyond that available to the sublessor but they thought that the existing law of contract, and misrepresentation, aided by modern New Zealand statutes dealing with breach of contract, misrepresentation and mistake, should be adequate to cope with such questions.

493 The Law Commission agrees with the views of the Committee and proposes a reform of the law along the lines which they have suggested, namely, that unless a contrary intention appears, a sublessor should be deemed to have a

reversion and that the sublease should not operate as an assignment. It could also be provided that, once the head lease is extended or renewed, the term of the sublease should *ipso facto* be extended to the earlier of (i) the expiry date of the extended head lease, or (ii) the expiry date expressed in the sublease.

Questions:

Q116 Should a sublease for the same or longer term than the lease out of which it is granted operate as a sublease rather than an assignment unless the parties intend otherwise?

Q117 Should it be provided that once the head lease is extended or renewed the term of the sublease should be extended as suggested in para 493?

HEAD LESSOR'S RIGHTS AGAINST SUBLESSEE AFTER MERGER

494 A person who has granted a lease may not deliberately destroy what has been created. Consequently, a voluntary surrender of the interest out of which the lease was granted (usually a head lease) is ineffective to put an end to that lease (the sublease) which is dependent upon it (*Mellor* v *Watkins* (1874) LR 9 QB 400). This is the case even where the sublease has been granted in breach of the head lease so that the superior landlord, instead of accepting a surrender, might have forfeited the head lease.

495 Upon surrender of the head lease the head lessor thereby gets no greater freedom in relation to the sublease than an assignee of the head lease would have had; it comes burdened with whatever sublease has been created by the lessee (*Wilson* v *Jolly* (1948) 48 SR(NSW) 460). What the sublessor surrenders to the head lessor is the reversion upon the sublease. At common law when the head lease was surrendered the reversion merged into the fee simple and was extinguished. Because the rent and the sublessee's covenants are incidents of the sublessor's reversion, the extinguishment of the reversion led to the inconvenient result that the head lessor could not claim the rental or enforce the covenants under the sublease (*Webb* v *Russell* (1789) 3 Term Rep 393; 100 ER 639). Yet the sublessee could remain in possession and enjoy the benefit of its lease. To avoid this difficulty the courts held that the sublessor could surrender only as much of the lease as was legally possible and therefore retained "a sufficiency of his reversion as regards the subtenant in order to support continuance of the latter's title" (*Wilson* v *Jolly* at 470). This interest is known as a continuance.

496 Legislation also came to the assistance of the head lessor. Section 111 of the Property Law Act is intended to give a head lessor or other person holding an interest in land into which another interest is merged at a time when that prior or lesser interest is already burdened with a lease, the

ability to enforce that lease. The former head lessor is to have "the same remedy for non-performance or non-observance of the conditions or covenants expressed or implied in the lease as the person who would for the time being have been entitled to the mesne reversion so merged would have had".

497 However, it is doubtful that the section presently gives the reversioner the ability to give a notice to quit so as to terminate a subtenancy which is in the form of a periodic tenancy. In *Wilson* v *Jolly* both the head lease (which was surrendered) and the sublease were periodic tenancies. It was held that the existence of the continuance enabled the head lessor to give a notice terminating *the head lease* (thus collapsing the dependent sublease) without notice to the sublessee, despite the fact that the head lease had already been surrendered.

498 However, this rather ingenious solution to the deficiencies of section 111 would not, it seems, assist the head lessor where the surrendered and merged head lease had been for a fixed term and only the sublease was a periodic tenancy.

499 It is suggested that section 111 be amended by specifically including amongst the rights of the reversioner the right to give any notice which the person who would for the time being have been entitled to the mesne reversion so merged would have been able to give.

500 It does not seem desirable to impose on the person who has received the benefit of the merger the obligations which the surrenderer undertook *to* the sublessee. On the other hand, as the section now does, it is reasonable for the surrenderee to have the benefit of covenants undertaken *by* the sublessee. The first case would render someone liable for obligations they had never agreed upon, whilst the second continues obligations already undertaken but gives the right of enforcement to a different person.

Question:

Q118 Should a reversioner of a head lease be empowered after merger to give notice terminating any periodic subtenancy created out of that head lease?

XVI
RESTRICTIONS ON DISPOSITION OR USER OF LEASED PREMISES

DISPOSITION

501 Sections 109 and 110 came into the Property Law Act at different times which is probably why they have remained separate sections. Section 109, which dates from 1905, prevents a lessor asking for a "fine or sum of money in the nature of a fine" in return for giving a consent where the lease contains a covenant, condition or agreement that the lessee shall not, without the licence or consent of the lessor, assign or sublet the premises. The covenant is deemed to be subject to a proviso to this effect.

502 Section 110, dating from 1936, converts a qualified covenant, ie, one preventing assignment, or subletting without consent, into a fully qualified covenant, namely one where the requirement for consent is deemed to be subject to a proviso that it is not to be unreasonably withheld.

503 These sections would, it seems to the Law Commission, be easier to comprehend if they were amalgamated. It could be provided in one section that every covenant against disposition without consent, ie, assignment, subletting, parting with possession or mortgaging the lease, should be deemed to be subject to provisos that:

- consent should not be unreasonably withheld by the lessor; and

- no payment of money (whether by way of additional rental or by way of premium or fine) or other consideration could be required as a condition of or in relation to the consent of the lessor. Any money so paid would be refundable upon demand.

504 In Australia it has been said that a "fine" does not include a requirement for an increase in rental payments (*Barina Properties Pty Ltd* v *Bernard Hastie (Australia) Pty Ltd* [1979] 1 NSWLR 480). The Law Commission's proposal would reverse this conclusion. However, reasonable costs incurred in relation to the consent by the landlord would still be claimable.

505 Section 109(2) is well known to conveyancers, if only because it is almost universally excluded in carefully drawn leases (including standard printed forms), a course which the subsection itself expressly permits. The subsection states that an assignment or subletting by an official assignee, liquidator or sheriff or a bequest of a lease is not to be regarded as a breach of a covenant against disposition. It seems rather pointless to repeat this subsection when, as we have said, it is virtually always excluded. In every case covered by the subsection there would remain at least three steps which could be taken by any affected party: the

assignment could simply be proceeded with, or an application could be made for an order that consent was being unreasonably withheld or, if the lessor had already treated the assignment as a breach and had purported to terminate the lease, an application could be made for relief under section 118. It seems to the Law Commission that these remedies are sufficient for the purpose and that section 109(2) should not be repeated.

506 It could well be provided that if the sole reason for the withholding of a consent is the existence of a liquidation, receivership or bankruptcy, the consent is deemed to be unreasonably withheld. This would not prevent a lessor from withholding consent because of a failure by the insolvent lessee to pay the rent or observe some other covenant.

507 In a decision of the Court of Appeal, *W E Wagener Ltd* v *Photo Engravers Ltd* [1984] 1 NZLR 412, a distinction was drawn between an attempt to avoid section 110 by defining in the lease what might constitute an unreasonable refusal, on the one hand, and the imposition of a precondition to any application for consent. It seems that the latter falls outside section 110. The Law Commission questions whether the distinction should be perpetuated. There would seem to be little difference in reality between, say, a provision that it is not unreasonable to require the lessee as a condition of consent to offer to surrender the lease to the lessor and a precondition that before any application for consent can be made, there must first have been an offer of surrender. The economic effect is the same. Therefore the Law Commission's present view is that in a case where the lessee is entitled to dispose of the lease with the consent of the lessor, a precondition of this kind should not be permitted.

508 Nevertheless, it has long been accepted that a lessor is perfectly entitled to contract on the basis of an absolute prohibition on disposition, though in practice this is relatively rarely found since lessees are very resistant to putting themselves in a position where they have no right of disposition unless the lessor, in its discretion, waives the covenant. Sections 109 and 110 are not intended to place any limitation on the operation of an absolute covenant against disposition and, if the parties are content to contract on this clear basis, there would not appear to be much case for changing the law to extend the new section to such a covenant. Nevertheless, we would be interested in hearing views on this point.

509 Though it would not, we think, involve any change in the law, the Commission thinks that there may be merit in following a suggestion recently made by the Law Commission of England and Wales and providing in the legislation for a right of action for damages by a lessee against the lessor where it is established that consent has been unreasonably withheld. It might also be usefully provided that a lessor must, upon request, give reasons for withholding consent.

Questions:

Q119 Should sections 109(1) and 110(1) be combined as suggested in para 503?

Q120 Should section 109(2) be repeated in the new Act?

Q121 Should the legislation forbid the attaching of a precondition to a consent to a disposition?

Q122 Should the rules now found in sections 109 and 110 extend to absolute covenants against disposition?

Q123 Should the legislation provide for an express right of damages for a lessee for breach of the section(s)?

Q124 Should a lessor be required, on request by the lessee, to give reasons for withholding a consent to a disposition?

USER

510 The Property Law Act now contains no provisions concerning the lessee's use of premises. Nothing in the Act stops the landlord from absolutely prohibiting any change of user. And if, instead, the lessee covenants not to change the use of the premises without the lessor's consent, the present law does not require the lessor to act reasonably in making up its mind whether or not to give a consent.

511 Three kinds of change of user clauses are commonly found in New Zealand. Many commercial leases (Building Owners and Managers Association form leases being the most notable example) contain an absolute prohibition on any change. Many other leases prohibit change without the consent of the landlord but do not require the landlord to act reasonably in determining whether to withhold consent or to impose conditions. A final group, rather less common than the others, do require the landlord to act reasonably in making a determination or imposing conditions.

512 The Law Commission observes that the fact that a lease very tightly restricts the use which may be made of premises and absolutely forbids any change may not always work to the advantage of the landlord. The tenant may point to its own disadvantageous state in this respect as a factor which should limit the amount of rent payable when the time comes for a rent review. Caselaw confirms that the tenant may thereby obtain a lower rent (*Plinth Property Investments Ltd* v *Mott, Hay & Anderson* (1979) 38 P & CR 361). However, this can be circumvented by the landlord if there is included the rent review clause, a direction that a valuer determining the new rent shall disregard restrictions in the lease relating to the use of the premises.

513 Another distinction, which was discussed by the Court of Appeal in *W E Wagener Ltd* v *Photo Engravers Ltd* [1984] 1

NZLR 412, is between the imposition of a condition as part of the process of the giving of consent (such as a condition that a certain type of activity shall be conducted only within limited hours) and the inclusion within the lease of a precondition, namely that a state of affairs must exist or a procedure must be gone through before the right to approach the landlord requesting a change of use ever arises. A device which is sometimes used is to insert a precondition that before the landlord may be asked for a consent to a change of user, the tenant must first have offered to surrender the lease. If, when such an offer is made, there is no requirement for payment of any consideration by the landlord so that the tenant must offer the surrender gratuitously, a precondition of this kind - currently uncontrolled in relation to assignments or user clauses, as was found by the Court of Appeal - can lead to abuse: the tenant may lose valuable goodwill attaching to the lease. This is particularly harsh if the tenant has paid goodwill upon entering into possession.

514 In England, section 19(3) of the Landlord and Tenant Act 1927, which is paralleled in some of the Australian jurisdictions, prevents the landlord levying a fine as consideration for a consent to an alteration of user. But it does *not* apply where:

- there is an absolute prohibition; or
- there is to be a structural change to the premises resulting from the change of user.

515 There seems to be no good reason for the second of these exclusions since a commercial lease will normally control by a separate covenant the ability of the tenant to interfere with the structure. So, if the tenant intended to change the use of the premises and to make structural alterations, the tenant would be required to get consent to both those actions. The fact that the landlord might by statute be required to consent to the change of user would not impact upon the landlord's ability to refuse consent to the alteration (*Barina Properties Pty Ltd* v *Bernard Hastie (Australia) Pty Ltd* [1979] 1 NSWLR 480).

516 The Law Commission of England and Wales in its Report No 141, *Covenants Restricting Dispositions, Alterations and Change of User* (1985) has reviewed section 19(3) and concluded that:

- a landlord should remain free to prohibit changes of use absolutely;
- the section should be extended to cover changes of user which also require structural alteration; and
- a "fine" should be defined in the widest possible terms and should include any increase in rent.

517 With all of these propositions we agree (on the assumption that there is to be a "user section" in New Zealand). The English Law Commission also made some further

recommendations which we are not presently disposed to recommend in New Zealand. They are that:

- The landlord's right to recover reasonable expenses should include a sum for compensation for diminution of value of the premises by reason of the change of user. However, it seems to us that this is a matter which goes to the reasonableness of the consent. It may sometimes (though, perhaps, not often) be reasonable that the tenant should be able to change the user even if that devalues the premises provided that proper compensation is paid. But if landlords are to be prohibited from demanding consideration in exchange for a mere change of user, the proposal seems to open up an immediate loophole whereby a landlord could demand money claiming that it was related to diminution in value. On the other hand, few landlords would be likely to agree to any proposal which they really thought would diminish the value of their properties. The question should be one for the general discretion of the court as part of its consideration of the overall reasonableness of the landlord's refusal. No compensation should be payable unless approved by the court.

- Provision should be made for statutory time frames within which the landlord must make a decision. However, it might be difficult to fix an appropriate period; a "reasonable time" should suffice and it is implicit that consent be given within a reasonable time. If consent were not so given, the landlord would be in breach and the lessee would have a right to damages.

518 Under the English legislation as it stands at present, if a tenant is unreasonably refused a change of user in a situation to which section 19(3) applies, the tenant can either apply to the court for a declaration or can proceed to change the use on the basis that the landlord's consent has been unreasonably withheld. The Law Commission of England and Wales thought (and we agree) that the latter right should be retained, but it does not seem to need legislation to confirm this rule.

519 In the same way as it is now impossible to contract out of sections 109 and 110 (except as to section 109(2)), we envisage that the parties would not be able to contract out of any new section on user.

Questions:

Q125 Should the new Act treat restrictions on user in the same manner as restrictions on dispositions?

Q126 If not, what differences should there be?

XVII
BREACH OF LEASE TERMS BY LESSEE

TERMINATION FOR BREACH BY LESSEE

520 The present law on re-entry, forfeiture and relief has been described by PLERC in its *Final Report on Legislation Relating to Landlord and Tenant* (1986) at para 93, as "a curious patchwork of old legislation, new legislation, and decisions based on the court's inherent jurisdiction to give relief against forfeiture".

521 We mention first the terminology in our proposals which follow. "Termination" would replace "re-entry and forfeiture" except when the physical act of re-entry is meant. We have chosen "termination" rather than "cancellation" (as in the Contractual Remedies Act 1979). They have the same meaning but "termination" is the word more frequently used in relation to the cessation of a lease. "Relief against forfeiture" would thus become "relief against termination". It should also be noted that a "condition" in this context is a condition of forfeiture, upon the occurrence of which the lease terminates or the lessee has the right to bring it to an end by notice. A common example is the insolvency of the tenant. A condition is distinct from a covenant: no damages claim follows breach of a condition.

Non-payment of rent

522 Section 118 requires a warning notice to be given before termination and enables the court to grant relief against forfeiture of the lessee's interest: but notice does not have to be given when the only default is non-payment of rent. A lease can at present provide for an immediate right to re-enter or the lessor can immediately apply for an order for possession if rent is not paid. In such cases the tenant may obtain relief against the forfeiture of the lease in the court's inherent equitable jurisdiction for up to six months after the re-entry. Alternatively, the tenant can forestall a possession order by paying the arrears of rent and costs in full before execution of the warrant: see section 32(3) of the District Courts Act 1947 or section 4 of the Landlord and Tenant Act 1730. These sections reflect the attitude of the Chancery Courts that the lessor's right to forfeit the lease for non-payment of rent is no more than a "security" for the rent.

523 The PLERC report recommended that the lessor should continue to have a right of re-entry or recovery of the property by court proceedings for non-payment of rent without formal demand after a period of 21 days (say, 15 working days). However, the Law Commission thinks that for the protection of sublessees and mortgagees of leases, there should be a requirement for a short period of notice - we suggest five working days - which could run *concurrently* with the 15 working days. Thus, the lessor could re-enter or seek a possession order once rent was in arrears for 15 working days *and* five working days' notice had been given.

524 Although the procedure for the giving of a notice under section 152 of the Act is mandatory in respect of section 118 and not without its difficulties (see paras 652 to 658), we think that in practice a problem with service is not very likely to be experienced in relation to a tenant, who will presumably be more easily found on the commercial premises or, at least, by inquiry at them, than is the case when a mortgagor has to be served. However, we would not wish to create a trap for a lay landlord who might reasonably conclude where the tenant appears to have abandoned the premises, leaving arrears of rent, that all that has to be done is re-entry and re-letting to a new tenant. For this reason we are inclined to the view that notice need not be given where:

- the rent is 15 working days in arrears; and
- the lessor reasonably believes that the lessee has given up possession of the premises; and
- the lessor does not have actual knowledge of the name and address of any mortgagee or sublessee.

This would legitimise the practice whereby in the event of abandonment of the premises, a landlord will usually re-enter without first giving any notice. No exception appears in section 118(1) but the practice accords with common sense and, as the law at present stands, perhaps can be legally justified on the basis of an actual or implied surrender.

525 Where there is a mortgagee or sublessee who is known to the lessor, then we propose that notice would need to be given to that party and section 152 would have to be complied with in respect of a notice to the lessee. This proposal links with the right of a mortgagee or sublessee to apply for relief against termination, which we discuss at paras 544 to 546 and 555 to 561.

Other breaches by lessee

526 Our suggested proposals to deal with a breach of lease other than non-payment of rent are broadly similar to the present section 118 and are incorporated in the following paras 543 to 554.

527 The lessor would (much as at present) be unable to exercise a right of termination for breach of any other express or implied covenant or condition unless:

- the breach is subsisting; and
- the lessor has given a reasonable period of notice to the tenant specifying the breach and requiring the lessee to remedy it; and
- the breach had not been remedied or reasonable compensation made before the termination.

The word "subsisting" is taken from *Bass Holdings Ltd* v *Morton Music Ltd* [1988] Ch 493 where it is contrasted with a breach which is "spent" despite never having been remedied.

528 The Law Commission has considered whether a fixed period of notice, like 20 working days, could be specified for breaches other than non-payment of rent but has concluded that such a period might be inappropriately short (or, less frequently, inappropriately long) in many situations. Consequently, although it will deprive landlords of the certainty of knowing exactly how long a period of notice must be given, it seems better to follow the existing section 118 in this respect.

529 We have also considered whether a lessor should be required to give notice where a breach of lease is incapable of being remedied. We see this question as very closely connected with the appropriateness of the lessee being allowed to "cure" the breach by offering compensation. If a breach has occurred and it is capable of being remedied the lessee should normally be required to do so. However, the lessor may indicate that it is prepared to accept compensation. In some cases (which it will be difficult to define) it may be unreasonable for the lessor to insist on the breach being remedied - compensation may be an appropriate substitute. But what if the breach is incapable of being remedied? This may, of course, demonstrate that the breach is so serious that it is reasonable for the lessor to insist on termination; but the fact that a breach cannot be remedied does not necessarily mean that an offer of monetary compensation will be inadequate recompense.

530 It is also necessary to understand what is meant by "incapable of being remedied". There are three situations. The first is where the breach involves the use of the premises for an immoral or illegal purpose such as brothel-keeping (*Rugby School (Governors)* v *Tannahill* [1935] 1 KB 87) or gambling (*Hoffman* v *Fineberg* [1949] Ch 245) or where the premises have otherwise been used in a manner which contravenes the law. Here the activities of the lessee are regarded by the courts as casting a stigma on the premises. The second category is breaches of a "once and for all" character. Once that has happened the lessee cannot reverse the situation - the continuing breach cannot be stopped (although eventually it may be spent so as no longer to be subsisting). This category includes some breaches which one might not ordinarily think of as being incapable of being remedied, such as an unauthorised subletting. It is said that this cannot be remedied once it has occurred even if the sublease is terminated (*Scala House & District Property Co Ltd* v *Forbes* [1974] QB 575). The practical consequence is that the lessor is not obliged to give a long period of notice in order that the lessee has time to remedy the breach. Presumably, where this may result in an injustice, it can be put right, if compensation is adequate, upon an application for relief against termination.

531 It seems to the Commission that breaches falling within the first (or stigma) category should not be regarded as

always uncompensatable. The courts may continue to take a strict view, as they have done in the past, but, if the requirement for the giving of notice is dispensed with, the lessee will *never* have the opportunity in such a case of forestalling termination by tendering compensation. The matter could then be determined only by an application for relief. The same applies to once and for all breaches; indeed it may be that some, like the unlawful sublease, demand only nominal compensation once the act complained of has ceased. In other situations it may be reasonable that the breach be allowed to continue with compensation being the "price" paid for that right.

532 The third category is the truly irremediable breach, which will be fairly rare (except for breaches of conditions of forfeiture relating to continuing solvency, eg, where the lessor has the right to terminate in the event of the lessee's bankruptcy). Even here there remains the possibility of annulment. Even where a truly irremediable breach occurs it may be that compensation will be adequate. Certainly we think that the lessee should have the benefit of receiving formal warning before the lease is terminated.

533 We are therefore inclined to the view that the notice should demand the remedying of the breach in all cases, if only because the lessor will often be unsure whether this is impossible. Section 118 already requires this. It is said that the lessee should always have the opportunity of considering whether to admit the breach; whether it is capable of remedy; whether to offer compensation, to try to make terms with the lessor; and whether to apply for relief (*Horsey Estate Ltd* v *Steiger* [1899] 2 QB 79, 91). The Commission also believes that the notice should draw the attention of the lessee to the possibility that the breach may be able to be cured in appropriate circumstances by an offer of adequate compensation. However, it is unrealistic to require the lessor in *all* cases to demand compensation: the lessor may find it impossible to frame a demand either because monetary compensation is inadequate or because it cannot accurately be quantified.

534 The lessor may correctly regard *any* compensation as inadequate. Section 118(1) appears to require a demand for reasonable compensation in money to the satisfaction of the lessor in all cases. But the courts have held that a lessor's notice is not invalidated by failure to claim it (*Lowe* v *Ellbogen* [1959] NZLR 103). The claim for compensation is treated as being a right given by statute to the lessor which may be waived. (In *Lowe* v *Ellbogen* the lessor was, however, held to have waived all right to compensation in respect of matters which were not complained of in the notice. But he could have damages for those that were stipulated and not remedied even though he did not claim compensation in the notice! This denial of compensation should, we think, be reversed by the proposed new section.)

535 Accordingly, though not without hesitation in what is a most difficult area, the Commission puts forward the

suggestion that in every case the lessor should specify the breach and require it to be remedied. The notice would not have to contain a demand for compensation but could do so. It should, however, contain mandatory statements that:

- where compensation is appropriate in whole or part, the breach may be remedied by an offer of adequate compensation; and

- the lessee may, in the event of termination of the lease, be entitled to relief against termination and should seek legal advice.

536 The notice would not inform the recipient whether, in the particular circumstances, compensation was in fact appropriate but it would alert him or her to the possibility that a tender of compensation might avoid termination or be taken into account on an application for relief. The risk involved in deciding whether to tender compensation instead of remedying the defect and in determining the quantum of any offer should fall on the lessee. The "safety net", if the lessee misjudges the situation, is the ability to apply for relief. A lessor who is in doubt about whether the lessee's offer is proper and adequate could apply to the court for a termination order, rather than re-entering.

537 The section could also state that a claim to compensation need not specify the amount and that an over-inflated claim would not invalidate the lessor's notice. Tender of reasonable compensation would be sufficient to meet it.

Notice to mortgagees

538 The present section 118(1A), which requires the lessor to give notice to a mortgagee of the lease, but does not invalidate termination for failure to do so, should be preserved. We think it should also require notice to be given to a sublessee of whom the lessor is aware. The sanction for a lessor's failure to give the notice would be damages - and the time limit for seeking relief against termination (para 546, below) could be extended.

Methods of termination

539 We suggest that the proposed new section should say that a lease could be terminated only by:

- peaceable re-entry without breach of section 91 of the Crimes Act 1961 (forcible entry); or

- order of the court.

540 If a re-entry were made in breach of this requirement, for example, a forcible re-entry, the lease would not be thereby terminated unless the lessee treated the re-entry as a repudiation and so cancelled the contract of lease. If the lessee did not cancel, there would nevertheless have been an

unlawful eviction and in accordance with our proposals in relation to that subject (paras 598 to 601), the rent would cease to be payable and the tenant's performance of other covenants would be suspended while the unlawful eviction continued.

541 The lease would, where the lessor sought a court order, continue in existence until the order was made. Termination should not, as it does under the existing law, back date on the making of an order to the date of the application to the court. Consequently the lessee would remain liable for rent (rather than mesne profits) and on the other lessee's covenants. That would in itself simplify the present law. The court could be given power to order payment of rent to the date of the order or such later time as possession is yielded up.

542 The Commission also suggests that the new section should provide that, where a lessor has commenced proceedings for an order terminating the lease, the right to that order should not be lost by acceptance of rent or other conduct unless the lessee reasonably believed that the lessor would then desist from seeking the order. Acceptance of rent would not in itself amount to waiver of the breach: compare section 122 of the Public Trust Office Act 1957.

RELIEF AGAINST TERMINATION

543 We consider that upon application by the lessee to the court, either in a separate application or in a lessor's action, the court should be able in its discretion to grant relief against termination upon terms and conditions. The relief section would follow the scheme of section 118(2) without altering its substance.

544 A mortgagee of the lease should also be entitled to claim relief. Presently, because of the way in which "lessee" is defined in section 117 (including "assigns"), a legal mortgagee seems to have standing but it is doubtful that a chargeholder does, despite section 118(1A).

545 The right to apply for relief should also exist where a lease is terminated because of the bankruptcy, receivership or liquidation of a lessee: see the definition of "bankruptcy" in section 117 and the reference to "condition" (that is, condition of forfeiture) in section 118(1). There is some discussion of the position of a lessee company in liquidation in *Jessett Properties Ltd* v *UDC Finance Ltd*, unreported, 17 June 1991, CA 179/90, where it is held that "bankruptcy" includes insolvent liquidation. A receiver or liquidator faced with the common lease condition by which the lessor may terminate in the event of a receivership or liquidation should now, it appears, be able to invoke section 118 by arguing that the condition is one of forfeiture. But we think that the point should be put beyond doubt.

546 One of the problems with the present section 118(2) is that there is uncertainty for the lessor over when the

lessee's right to seek relief lapses and, consequently, when the lessor can safely relet. The Commission suggests that an application for relief by a lessee or a mortgagee should have to be brought within three months of termination by re-entry. But where the lessor seeks a court order for forfeiture of the lease, the application should have to be made before the lessor obtains actual possession of the premises pursuant to the court order. In the case of termination by way of a court order, the current law is that relief must be applied for prior to the lessor's obtaining of possession by that means (*Rogers* v *Rice* [1892] 2 Ch 170). Presently the period for the making of an application where there has been a re-entry on the ground of non-payment of rent is six months. (No period is specified in respect of other breaches but six months is applied by analogy.) This ought, we think, to be standardised with the period of three months in section 121 (relating to relief against a refusal to renew, etc): see para 565. But the court should have power to extend the time limit where the application is made by a mortgagee who has not been served by the lessor with notice of intention to terminate (see para 538).

547 The court should be empowered in its discretion to give relief even where the breach is of an essential term. In *Shevill* v *The Builders Licensing Board* (1982) 149 CLR 620 and subsequent cases in Australia the right of lessors, who have terminated leases for non-payment of rent, to pursue the lessees and guarantors for damages has been questioned (it being said that there had in some of the cases not been a breach of a character sufficiently serious to enable termination for breach at common law). It has therefore become the practice in well drawn commercial leases to provide that certain breaches, including non-payment of any rental instalment, are breaches of essential terms. Currently, relief against forfeiture for non-payment of rent where there has been a peaceable re-entry depends upon the inherent equitable jurisdiction of the court. Relief against a forfeiture would not normally be available in equity in a case of non-payment of money on due date where time is essential. Although the jurisdiction in relation to non-payment of rent would under our proposals now become statutory, it seems desirable to make an express statement that relief is available where an essential term has been broken, but in the discretion of the court.

548 The new relief section could usefully state that an application for relief may be made without any admission as to the validity of the lessor's notice. As the law at present stands, the lessor is placed in a dilemma, as discussed in *Besseling and Bracegirdle* v *Bali Restaurant Ltd* (1981) 1 NZCPR 294, since an application for relief constitutes an admission that the lease was validly forfeited.

Cases of non-payment of rent

549 Section 4 of the Landlord and Tenant Act 1730 provides that when the landlord has brought proceedings for forfeiture based entirely on non-payment of rent, the tenant may

forestall forfeiture by paying the outstanding amount before an order is made by the court (ie, before the lease comes to an end). Section 32(3) of the District Courts Act 1947 is to like effect. There seems to be no need to carry forward any such provision because we think that, in practice, the court will very rarely refuse to grant relief against forfeiture for non-payment of rent if the arrears of rent and the landlord's costs and expenses are tendered, the exceptional case being where the tenant is a persistent offender in this respect. If the landlord is seeking an order for possession the court will in the ordinary case refuse such an order. A tender of all arrears and expenses will effectively produce the result now required by sections 4 and 32(3) unless there are exceptional circumstances. The existing lease will continue and there will be no need for any regrant. The possibility that a persistent offender may be refused relief will also be salutory.

Joint tenants

550 Where two or more persons hold a lease as joint tenants and one of them does not wish to apply for relief under section 118(2), the other(s) cannot do so, not being "the lessee" (*T M Fairclough & Sons Ltd v Berliner* [1931] 1 Ch 60). This rule should be overturned. The question whether an application by less than all the former tenants might unreasonably prejudice the lessor is a matter which could be considered by the court in the exercise of its discretion.

Licences

551 The operation of the section could be extended to contractual licences to occupy land which are often difficult to distinguish from leases (eg, *Hull* v *Parsons* [1962] NZLR 465 - a sharemilking agreement held to be a licence). Where such a licence is terminated for breach it seems to the Law Commission that the same rules as to notice and relief should apply as with a lease, though it would need to be made plain that a grant of relief did not create a proprietary interest in the licensee.

No contracting out

552 The substance of section 118(8), which prevents contracting out, should be preserved. The new section could well include an express prohibition upon any device which is an attempt to defeat the section. For example, there is sometimes found in commercial leases in New Zealand a clause which purports to give the lessor the right, in the event of default on any of the lessee's covenants, to convert the lease into a monthly tenancy. This device was held to be ineffective in *Holden* v *Blaiklock* [1974] 2 NSWLR 262 where it was said that its intention was to cause the balance of the term to disappear and to be replaced by the periodic tenancy, which was to arise when the lessor's notice was given. It therefore gave the lessor a right of forfeiture or breach and so was caught by the equivalent of section 118(1). Likewise in *Plymouth Corporation* v *Harvey* [1971] 1 WLR 549, where the

tenant had been obliged to deliver into escrow a signed surrender of the lease, which was to be released to the lessor if the lessee failed to comply with a covenant, the arrangement was found to be a device - a forfeiture in the guise of a surrender which remained a forfeiture for the purposes of the section. Such devices should be stated to be ineffective in clear language.

Code

553 The Commission intends that its proposals for termination and relief would constitute a code on the subject and that the inherent jurisdiction of court to grant relief would be excluded, ie, relief could not be given except in terms of the new section. In England it appears that the equitable jurisdiction to relieve from forfeiture against the wilful breach of covenant (other than a covenant for payment of rent) has been extinguished by section 146(2) of the Law of Property Act 1925 (*Billson* v *Residential Apartments Ltd, The Times* 26 February 1991). This is despite the fact that section 146(2), unlike our section 118(2), does not extend to a peaceable re-entry without court order.

Prejudicing the landlord's title

554 An unusual and archaic rule stands outside the rules concerning termination and relief and should, we think, be brought within them. A tenant who does anything which prejudices the title of the landlord forfeits the lease. The landlord may simply re-enter without notice. The history of the rule is set out in *Warner v Sampson* [1959] 1 QB 297 in the judgment of Lord Denning at 312-316. In feudal times when a lord allotted a feud or fee to a tenant, there was annexed to it an implied condition that the tenant should do service faithfully to him by whom the lands were given. In case of breach of the condition - and of the tenant's oath of fealty - the lands reverted to the lord who granted them. Forfeiture can occur if the tenant denies the title of the landlord by claiming that it is vested in the tenant or a third party or if the tenant assists a third party to set up an adverse title (Hill & Redman at para [2181]). It appears that section 118 (like its English equivalent, section 146(1) of the Law of Property Act 1925) does not interfere with this rule: the landlord claims forfeiture on the basis of an *implied* condition of forfeiture. The Commission suggests that the new sections dealing with termination and relief be worded to cover both covenants and conditions express or implied.

Questions:

Q127 **What period of time (if any) should be required to elapse before action may be taken to terminate a lease for non-payment of rent?**

Q128 **Should prior notice be required before a right of termination is exercised for non-payment of rent and, if so, what period is appropriate?**

Q129 Should notice of intention to terminate for breach have to be given in all circumstances including when the lessee has apparently vacated?

Q130 What form should a notice to a lessee take where a breach was incapable of being remedied or where compensation might be an appropriate "cure"?

Q131 What time limit (if any) for a relief application should be imposed?

Q132 Should section 118 be extended to licences to occupy land?

Q133 Should the holder of a mortgage or charge over a terminated lease be able to seek relief?

Q134 Is there need to re-enact section 4 of the Landlord and Tenant Act 1730 and section 32(3) of the District Courts Act 1947?

Q135 Should the inherent equitable jurisdiction of the court be excluded?

RELIEF FOR SUBLESSEES

555 Section 119 authorises the court, where a lessor is enforcing a right of re-entry or forfeiture, to make an order vesting all or part of the premises in a sublessee upon such conditions which the court may impose. The period during which relief can be claimed should be the same as the period adopted in the new section 118 (three months being our suggestion), with provision for extension of time by the court if the lessor fails to notify the sublessee of its actions as required by that section. Currently the sublessee loses the right to apply under section 119 as soon as the head lessor regains possession (*Rogers v Rice* [1892] 2 Ch 170).

556 The current legislation does not stipulate that where a head lessee gets relief under section 118, any sublease and interest or rights deriving from it are to be reinstated without regrant. This might be spelled out. It might in some circumstances avoid the need for an application under section 119.

557 Section 119 has been interpreted as giving the court very wide powers to make adjustments between the head lessor and the sublessee appropriate to the circumstances, which can themselves vary considerably from case to case. For example, the sublease may be only a small part of an extensive head lease. In those circumstances it may be unreasonable to inflict on the head lessor a direct tenancy of that small part (*Chatham Empire Theatre (1955) Ltd v Ultrans Ltd* [1961] 2 All ER 381). Likewise it may be inequitable to force upon the head lessor privity of contract with a person whom the head lessor would have been entitled to refuse as a tenant if application for consent to a sublease or an assignment had

been duly made (*Creery* v *Summersell and Flowerdew & Co Ltd* [1949] Ch 751). There would seem to be little advantage in attempting to define the way in which the broad discretion of the court might be exercised beyond the guidance now found in section 119.

558 The new section could empower the court to make its order retrospective. Because an order under section 119 is a new grant (*Cadogan* v *Dimovic* [1984] 2 All ER 168) the court does not have power to give a successful sublessee the benefit of the sublease from date of re-entry under the head lease until the date of the grant of the new lease under section 119 (*Official Custodian for Charities* v *Mackey* [1984] 3 All ER 689).

559 Surprisingly, there is no express power in the present section for the court to order the lessor to execute a new lease to the sublessee (*Official Custodian for Charities* v *Mackey*). The Law Commission believes that this should be plainly stated.

560 There is no need for the head lessee to be brought before the court unless the court so orders, because the form of the relief does not involve reinstatement of the head lease and therefore no new liability is thrown on the head lessee (*Belgravia Insurance Co Ltd v Meah* [1964] 1 QB 436). The new section could contain a provision to this effect.

561 By virtue of the definition of "underlessee" in section 117 an application under section 119 can be made by a person deriving title through or from a subtenant. A chargee, though deriving title through the subtenant, has no agreement for the grant of a leasehold interest, which is required in the definition of "underlease". Especially if, as we suggest, all land mortgages are to take effect as charges only (see para 270), the right of a chargee to claim relief should be given. A new lease vested in a mortgagee is treated as a substituted security and is subject to the former subtenant's equity of redemption (*Chelsea Estates Investment Trust Co Ltd* v *Marche* [1955] Ch 328).

Questions:

Q136 Should the court have power to make a retrospective order in favour of a sublessee?

Q137 Should a mortgagee (chargee) of a sublessee be able to apply for relief?

RELIEF AGAINST REFUSAL TO GRANT RENEWAL ETC

562 Section 120 empowers the court to grant relief to a lessee who has lost the right to renew the lease or acquire the lessor's interest because the lessee has failed to give an effective notice exercising the right or because the lessee

has failed to comply with a precondition to that exercise. But the right to apply for relief exists only during the three months' time limit in section 121.

563 It is our impression that since section 120 was redrafted in 1976 it has worked reasonably well. We would be interested in comments on this observation. However, the Law Commission suggests that the following adjustments could be made:

- The definition of "lease" could be extended to cover a licence to occupy. This would reverse *Hull* v *Parsons* [1962] NZLR 465 in which a sharemilker was denied relief under section 120 because the sharemilking agreement was a licence rather than a lease, ie, it did not give exclusive possession of the farm in the particular circumstances of the case.

- The opening portion of subsection (3)(a) could read:

  "Where a lessor has covenanted or agreed in writing with a lessee ..."

This change would mean that the lessor's covenant did not have to be contained in the lease itself, so, if the lessee had separately negotiated a right of purchase, relief would be available in respect of it.

Time limit

564 The major difficulty with section 121 is that it is all too easy for a lessee or its adviser to overlook the time limit. In small part this may be because the word "may" in the second line of subsection (1) looks permissive rather than mandatory. It ought to be replaced with "must". But the real cause is often ignorance or forgetfulness of the existence of the section, or failure to realise that time is running under it.

565 In the case of section 118 the time limit which the Law Commission is proposing (para 546) would not run unless there had been an actual re-entry so that the lessee is physically taken out of possession. However, in the case of section 120 there may have been no physical change but merely a communication, the significance of which is lost on a lay lessee. For this reason it is suggested that section 121 should be amended so that the three months' time limit (which seems sufficiently long if this reform is adopted) does not begin to run until there has been a communication which expressly directs the attention of the lessee to the time limit. By "expressly" we mean that the notice would have to point out the existence of the right to apply for relief and to warn the lessee that it lapses three months after the date on which the notice is received by the lessee.

Questions:

Q138 **Should section 120 be extended to licences to occupy land?**

Q139 **Should the section operate when the lessee's right is found outside the lease document?**

Q140 **Should the Act require the notice to the lessee to be more explicit concerning the right to relief and the time limit?**

XVIII
MISCELLANEOUS REFORMS TO LAW OF LEASES

DISTRESS FOR RENT

566 Distress for rent is already abolished in New Zealand in respect of all dwelling-houses: see section 107A of the Property Law Act 1952. In 1986, after issuing an interim report, conducting extensive consultation and receiving submissions on the question, PLERC in its *Final Report on Legislation Relating to Landlord and Tenant* recommended the abolition of the right to distraint in all other cases. The numerous submissions made to that Committee were overwhelmingly in favour of abolition. The Law Commission in England has recently made a similar recommendation (*Landlord and Tenant: Distress For Rent* (Law Com No 194, 1991)). It saw distress as

> wrong in principle because it offers an extra-judicial debt enforcement remedy in circumstances which are, because of its intrinsic nature, the way in which it arises and the manner of its exercise, unjust to the debtors, to other creditors and to third parties. (para 3.2)

567 The report quotes approvingly these comments of Sir Jack Jacob, *The Fabric of English Civil Justice* (1987) at 179:

> Distress for rent is an archaic, feudal survival, which has no place in a mature legal system. It is encrusted with technicalities, and the law relating to it "constitutes a veritable jungle of rules and exceptions". It is discriminating in giving the landlord rights which other creditors do not enjoy and in placing the tenant in greater peril than other debtors. It is an arbitrary, high-handed and summary process ...

568 Distress was abolished in New South Wales, Victoria, Queensland and Western Australia many years ago: see Landlord and Tenant Amendment (Distress Abolition) Act 1930 (NSW); Landlord and Tenant Act 1958 (VIC); Property Law Act 1974, section 103 (QLD) and Distress for Rent Abolition Act 1936 (WA). It has been recommended for abolition in South Australia (see Report 66 of the South Australia Law Reform Committee: *Relating to the Reform of the Law of Distress.*)

569 Although the right to distrain was once an essential ingredient of the relationship of landlord and tenant, that is no longer so; indeed it is not looked upon with favour by the courts. The Law Commission considers that distress for rent should be entirely abolished. This would involve repeal of several of the surviving Imperial statutes together with the Distress and Replevin Act 1908.

WASTE

Types of waste

570 Waste is a tortious act or omission whereby the nature or character of premises is altered in a permanent way to the prejudice of the person entitled to the immediate reversion (*Woodhouse* v *Walker* (1880) 5 QBD 404). It may involve action taken by the tenant in relation to the premises (in which case it is called voluntary or commissive waste) or may be failure to prevent dilapidation (permissive waste). The other category of waste is equitable waste, which happens only where a tenant is granted the right to commit waste ("without impeachment for waste") but does, in relation to the premises, a particularly flagrant act of destruction which is not covered by the dispensation. So called ameliorating waste, in which the character of the land is altered but its value increased by the alteration, is not waste at all, for no tort is thereby committed.

Relationship of waste to lease covenants

571 As waste is a tort, its commission is not dependent upon the terms of the contract between the landlord and the tenant but those terms will ordinarily delimit or qualify the tenant's tortious liability. It is as yet unclear whether, in the event that the tenant's contractual obligations are the same as or greater than those which the law of waste would impose, the liabilities exist alongside one another: see the contrasting views expressed in *Mancetter Developments Ltd* v *Garmanson Ltd* [1986] 1 All ER 449 at 454 and 456. However, in *Regis Property Co Ltd* v *Dudley* [1959] AC 370 Lord Denning treated the remedies as cumulative. Inconsistencies are (and we think should be) resolved in favour of the contractual arrangements:

> A man cannot commit waste, even technically, if he is doing that which he is entitled to do by contract - that is to say, he cannot commit waste as against his landlord if his landlord has entered into a special contract enabling him to do it (*Meux* v *Cobley* [1892] 2 Ch 253, at 262-263, Kekewich J).

Permissive waste

572 Before the Statute of Marlborough 1267 (52 Hen 3, c 23) an action in waste lay only against a tenant whose estate was created by law, not by grant from a landlord. The statute extended the common law liability to all tenants although, strangely, it is still not entirely settled whether a tenant is liable for permissive waste (Woodfall at para 1-1526).

573 In modern times an action for permissive waste is a rarity since liability for deterioration is usually addressed in the express terms of the lease or under an implied covenant. It will become all the more so if our proposals for implied covenants relating to repair are adopted (paras 408 to

410). The Law Commission believes that the tort of permissive waste can be safely abolished. This proposal assumes that a new Act will contain an implied repair obligation in long-term leases.

Voluntary waste

574 For the same reason an action for voluntary waste has become uncommon but the existence of the tort is occasionally of some real benefit to a landlord, as was evidenced in *Mancetter Developments Ltd* v *Garmanson Ltd* where a director of a tenant company was found liable and ordered to pay damages because he had caused the company to commit voluntary waste (removal of trade fixtures without reinstatement of holes made in the outside walls during their installation). The landlord's contractual remedy against the company was useless because the company had become insolvent.

575 The law of voluntary waste has also been found to be relevant in New Zealand in relation to tenants who have improperly cut standing timber. A line of New Zealand cases establishes that a tenant may not cut timber where land is leased for farming purposes unless the land would be of no practical use to the tenant for farming were the timber not cleared away (see *Gardner* v *Hirawanu* [1927] AC 388 (PC)).

576 Our conclusion is that the law of voluntary waste can continue to play a useful role (but one which is consistent with the lease contract) and should be preserved. However, a claim should not succeed against an agent if the principal has not breached the terms of the lease. The new Act should make this clear: if by contract the tenant may do something which would otherwise constitute waste, an agent of the tenant who does that act for the tenant should not be chargeable with waste.

Equitable and ameliorating waste

577 Equitable waste in its particular and, in New Zealand, unusual circumstances is also worth preserving. This could be done by extending section 29 of the Property Law Act to leases.

No criminal liability

578 In view of section 106 of the Crimes Act 1961 (imposing a criminal penalty for contravention of any statute which prohibits the doing of any act) it may be thought prudent to confirm (as does section 24(3) of the Property Law Act 1974-1986 of Queensland) that there is no criminal liability for waste. We should not be taken to endorse section 106 - quite the contrary - but it is beyond the scope of this paper.

Liability for fire damage

579 One further point seems to require attention. Section 86 of the Fires Prevention (Metropolis) Act 1774 provides a

defence to an action for damage resulting from a fire which begins "accidentally" on premises. It seems that one reason for the enactment of this legislation may have been that a tenant could at common law be found liable for waste where a building had been destroyed by fire or lightning, without fault of the tenant, but the tenant had not reinstated the premises within a reasonable time (*Rook* v *Worth* (1750) 1 Ves Sen 460). Section 86 can now be repealed and the common law rule, having been abolished by the 1774 statute, will not then be revived by repeal of that Act: see Acts Interpretation Act 1924, section 20(f), and Imperial Laws Application Act, section 3(4).

Liability of co-owners for waste

580 Here we depart for a moment from the law relating to leases in order to complete our discussion of waste. The Queensland Law Reform Commission in its Working Paper WP30 published in 1986 has recommended inserting into the Queensland Property Law Act a section in the following terms:

> A co-owner who unlawfully commits voluntary waste is liable in damages to any other co-owner of the property in proportion to the interest of that other co-owner in the property.

581 The commentary on the clause states that, apparently, an action for waste by one co-owner against another would not lie at common law but was expressly conferred by a section of the Statute of Westminster the Second (13 Edw 1), namely c 22. The statute was entirely repealed in New Zealand by the Imperial Laws Application Act 1988. The report of the Justice and Law Reform Committee on that Act does not comment on c 22. But Hinde McMorland & Sim at para 12.031 confirms that the right of a co-owner to sue another co-owner for waste was based on it.

582 The Queensland Law Reform Commission notes that it is at least arguable that an action for waste between co-owners is still available despite repeal of the statute but considers that the Queensland Property Law Act should clarify the position. We agree that the New Zealand Act should do so, on the assumption that the torts of voluntary and equitable waste are to continue as part of our law.

Questions:

Q141 Should the tort of permissive waste be abolished?

Q142 Should the tort of voluntary waste be abolished?

Q143 Should the tort of equitable waste be abolished?

Q144 Should one co-owner be made liable to other co-owners for waste?

DURATION OF TERM OF LEASE: THE REQUIREMENT OF CERTAINTY

583 One of the formal requirements for the creation of a valid fixed-term lease is that it is certain as to term both in respect of commencement and termination dates. If the term is not certain, then a good leasehold interest has not been created. The grant will offend the principle that only an estate of freehold may be of uncertain duration: it will therefore be void. As a result a lessee relying on it may be found to be in occupation of the premises on the basis of a statutory monthly tenancy only.

584 The common law requires that the duration of the lease must be certain when it commences. This causes difficulty when future circumstances are used to fix the date of termination. The problem achieved a certain legal notoriety during World War II when it became common in England and New Zealand to let premises for the "duration of the war". In *Lace* v *Chantler* [1944] KB 368 such a grant was held to be invalid because the duration of the war was uncertain. The rule approved in *Lace* v *Chantler* has been approved in New Zealand in two decisions, one of which also involved a lease entered into during the war (*Mrs Levin Ltd* v *Wellington Co-operative Book Society* [1947] NZLR 83 and *Sinclair* v *Connell* [1968] NZLR 1186).

585 Both in England and New Zealand, as a result of the decision in *Lace* v *Chantler*, legislation had to be passed validating the many leases which were affected. Thus, as a matter of policy, in both countries it was recognised that here was a circumstance that did not justify the application of the rule. If it was thought appropriate to validate these leases, the Law Commission does not find it easy to see why the rule should not be generally dispensed with, for the consequences of failure to observe the rule may be equally harsh in other circumstances. Moreover, a careful drafter can avoid the effect of the rule whilst achieving the same result as was intended in *Lace* v *Chantler*. All that is required is to specify an ultimate termination date at a point well beyond the expected occurrence of the movable event, with a further provision that on the occurrence of the movable event the lease will come to an end. So the termination date is the specified date or the future event, whichever is the earlier.

586 It seems to the Law Commission that a lease should be regarded as certain if the future event which is used to define its termination date is sufficiently described as to be identifiable when it occurs. However, there is still the possibility that the prescribed event may be one that may *never* occur. Consequently legislation to change the rule exemplified in *Lace* v *Chantler* would need to prescribe an arbitrary termination date to apply if the parties to the lease do not themselves prescribe a backstop finite date. We suggest that the fifth anniversary date of the commencement of the lease might be a suitable statutory backstop date.

587 It would also be necessary to specify in any new section of the Property Law Act effecting these reforms that nothing in the section affected the law relating to periodic tenancies, since it is established by caselaw that it is unnecessary to specify a termination date for them, it being sufficient that either party can bring the periodic tenancy to an end by giving the appropriate period of notice (*Re Midland Railway Co's Agreement, Charles Clay & Sons Ltd* v *British Railways Board* [1971] Ch 725).

Questions:

Q145 Should it be possible to create a valid lease to terminate on the occurrence of a specified and recognisable future event?

Q146 If so, should the legislation specify a statutory backstop date (five years) to apply if the parties do not provide their own backstop date?

REMOVAL OF FIXTURES BY LESSEE

Characteristics of fixtures

588 A chattel which a tenant affixes to land permanently or temporarily loses its character as a chattel and becomes part of the land. When a chattel is so attached to the premises by a tenant as to become an integral part of them - part of the structure of a building - it is categorised as a *landlord's fixture*. Then the tenant has no right to remove it. But an item affixed by a tenant, but not so as to become a landlord's fixture, is classified as a *tenant's fixture* and, subject to the terms of the lease, will be removable during such period as the relationship of landlord and tenant continues. In this circumstance, although the chattel has become part of the land by being affixed to it and, while affixed, belongs to the landlord, so that the landlord's mortgagee may sometimes be able to claim it, the tenant does not usually lose the right to recover ownership until the lease ends.

589 Tenant's fixtures are a (now very wide) exception to the general rule that chattels attached to the land belong to the landlord as part of the land and are not removable. The exception was developed by the courts for the protection of business tenants and the encouragement of trade. A chattel affixed for the purpose of trade is called a trade fixture and is removable by the tenant unless it has become a landlord's fixture in the sense mentioned above.

590 In the same way ornamental fixtures installed by a tenant of a residential property are removable. This rule is

of comparatively little importance in New Zealand at the present day except in relation to long-term residential tenancies, ie, those for five years or more, since the right of any other residential tenant to affix and remove fixtures is now governed entirely by section 42 of the Residential Tenancies Act 1986.

Lapsing of right to remove fixtures

591 The Law Commission is aware of two serious problems in the law relating to tenant's fixtures. The first derives from the rule that the right to remove them generally lapses and they become entirely the landlord's property once the landlord and tenant relationship ceases, although the law on this point has been liberalised by *New Zealand Government Property Corporation* v *H M and S Limited* [1982] QB 1145. It was there held that when a lease expires and the tenant remains in possession by virtue of a new grant or a holding over, the tenant does not lose the right to remove tenant's fixtures. Where the lease comes to an end suddenly, such as on a re-entry by the landlord after breach of the lease by the tenant, the law allows the tenant a reasonable period to remove his or her fixtures. But if the tenant has to vacate at the end of the term there is a difficulty, for then no reasonable period is allowed after the end of the lease for removal.

Agricultural fixtures

592 The second problem is caused by the fact that the common law exception for trade fixtures does not extend to fixtures installed by an agricultural tenant (*Elwes* v *Maw* (1802) 3 East 38; 102 ER 510). This was remedied by section 3 of the Landlord and Tenant Act 1851 (14 & 15 Vic c 25) which empowers agricultural tenants to remove certain agricultural fixtures, including buildings, engines and machinery and remains in force in New Zealand (Imperial Laws Application Act 1988, First Schedule). However, the right which the section grants is much more limited than the right given at common law to tenants of other types of property because of certain statutory conditions of removal, namely:

- the landlord must have given written consent to the annexation of the chattel;
- the tenant must have paid for the annexation;
- the tenant must give the landlord one month's notice of removal;
- the landlord has the right to purchase the fixtures at a price to be fixed in accordance with a formula in the section; and
- the tenant must not injure the land or any building of the landlord or else must make good such damage in effecting the removal.

593 The Law Commission has the impression that lessees of New Zealand farms and their advisers do not place much (if any) reliance upon this Imperial Act; that people taking leases of farms either ensure that they have express written agreement enabling them to remove fixtures or incorrectly rely upon the general exception for trade fixtures without realising that it does not apply.

Proposals

594 PLERC's *Final Report on Legislation Relating to Landlord and Tenant* (1986) recommended that there should be a general rule that any commercial or farm tenant might remove fixtures within a reasonable time after the termination of the lease and that there should be a rebuttable presumption that removal was reasonable at any time until the tenant actually vacated the property (irrespective of the capacity in which the tenant remained in possession). This, it was thought, would give courts the power to foreshorten the period in cases where the tenant clearly knew that the tenancy had come to an end and to extend the period where the tenant gave a reasonable explanation for the delay.

595 The Committee also thought that it was unnecessary to have a separate regime for agricultural fixtures, which it thought should be treated in the same way as trade fixtures.

596 We are inclined to agree with these suggestions. As to the first: we were, to begin with, impressed with the idea that there may be advantage to all concerned if a finite period, say 20 working days, is fixed by the statute, being a period during which trade, ornamental and agricultural fixtures can be removed *after* the relationship of landlord and tenant has come to an end. There could also be a right for a tenant to apply to the court for an extension of time where circumstances prevented the right being fully exercised during the 20 working days.

597 However, on further reflection we think that the time limit of 20 working days may often be inappropriate and that it might be better if the new Act said that a lessee will have a reasonable time after ceasing to have legal possession in which to remove tenant's fixtures, leaving it to the court to say what is reasonable in particular circumstances.

Questions:

Q147 Should agricultural fixtures be treated any differently from commercial fixtures?

Q148 Should a tenant have a period of time after termination of the lease in which to remove fixtures?

Q149 If so, should the Act refer to a "reasonable time" or fix a period of time, with power to the court to extend it?

EFFECT OF UNLAWFUL EVICTION UPON RENTAL

598 A tenant unlawfully evicted by the landlord is not liable to pay rent which accrues after the eviction and while it continues (*Boodle* v *Campbell* (1844) 7 Man & G 386; 135 ER 161 and *Reid* v *Finer* (1913) 32 NZLR 1213). While that rule is clearly fair, an eviction from *part* of the premises also suspends the *whole* of the rent even if the tenant continues to enjoy the use of a substantial portion of the premises (*Morrison* v *Chadwick* (1849) 7 CB 266; 137 ER 107 and *Orr* v *Smith* [1919] NZLR 818). That rule may be unfair to the landlord, particularly where the eviction relates to a relatively unimportant portion of the premises.

599 Curiously, if the eviction comes about because a person with a title superior to that of the landlord requires the tenant to vacate part of the premises (or, alternatively, to become the tenant of that person), the court will make an equitable adjustment of the rent, requiring the tenant to pay a fair rent in respect of continuing occupation of the balance of the property of which the tenant has undisturbed possession (*Tomlinson* v *Day* (1821) 2 Brod & Bing 680; 129 ER 1128).

600 But in circumstances in which the tenant is unable to enter the entire property at the commencement of the lease because part of it is still in the possession of someone who has been granted an earlier lease by the landlord, the court will *not* apportion the rent (*Hughes* v *Mockbell* (1909) 9 SR (NSW) 343). A further anomaly is that the landlord may be entitled to demand the *entire* rent where the second lease is granted out of the landlord's reversion and can operate as a concurrent lease; and it seems that this may be so even if the tenant was expecting to be able to go into actual possession: see the discussion, and divergent views, in *Hughes* v *Mockbell*.

601 The view of the Commission is that the proposed new Property Law Act should rationalise this rather confused state of affairs by providing that:

- upon a total eviction the rent and other obligations of the lessee cease during the period throughout which the eviction continues;
- there should be an apportionment of the rent and other obligations during a partial eviction;
- the rules should be the same if the lessee is unable to enter into possession at the beginning of the lease;
- the lessee should have the right to terminate the lease if the lessor has repudiated the lease contract by evicting the tenant or the eviction is sufficiently serious to pass the substantiality test in the Contractual Remedies Act; and

- where in these circumstances the performance of the lease by the lessee is dispensed with, the lessor should not be able to claim in respect of the non-performance against an assignor or guarantor of the lease.

Question:

Q150 Should the law relating to evictions be reformed in the manner outlined in para 601?

STATUTORY TENANCIES

602 At common law, if there was a lease, including a holding over, but no express or implied agreement between the parties that it was to continue for a term of years or that it was to be at will or on a periodic basis then, although the lessee might have entered as an implied tenant at will, when rent was to be paid calculated on an annual basis, the tenancy ceased to be a tenancy at will and became a tenancy from year to year (*Dockrill* v *Cavanagh* (1944) 45 SR (NSW) 78, 83).

603 Section 105 of the Property Law Act 1952 provides:

> No tenancy from year to year shall be created or implied by payment of rent; and if there is a tenancy it shall be deemed in the absence of proof to the contrary to be a tenancy terminable at the will of either of the parties by 1 month's notice in writing.

604 This section has never been definitively interpreted by the Court of Appeal although there have been many first instance decisions on it. The generally accepted view is that of Edwards J: that it abolishes all tenancies by implication of the law and replaces the difficult and complicated rules which prevail at common law with one uniform rule for the determination of the nature of all indefinite tenancies (*Tod* v *McGrail* (1899) 18 NZLR 568, 572).

605 In Australia, however, a more restricted view has been taken of the equivalent section, namely that it is inapplicable unless at common law the tenancy in question would have been treated as a tenancy from year to year (*Burnham* v *Carroll Musgrove Theatres Ltd* (1927) 28 SR (NSW) 169, affirmed 41 CLR 540). The Law Commission thinks that to put this matter to rest it is desirable that section 105 be rewritten so as to confirm the view taken by the New Zealand courts.

606 At the same time, however, care should be taken to ensure the section is redrafted in language which, while appropriate for the creation of a presumption of law, does not preclude the ability of the court to imply as a matter of fact a tenancy of a different duration where that is warranted by the circumstances. For example, in the same way as section

105 can be excluded by express agreement that the tenancy shall be terminable at will or on a particular period of notice or at a particular time, it should continue to be left open to the courts to imply any of those terms as a matter of factual implication (see *Ormond* v *Portas* [1922] NZLR 570 and *Beattie* v *Lyttelton Borough* [1966] NZLR 65).

607 Section 105 is not applicable in the case of a residential tenancy: section 142 of the Residential Tenancies Act. This would continue to be the case.

Question:

Q151 Should it be confirmed that there can be "statutory tenancy" regardless of whether at common law there would have been a tenancy from year to year?

ACTIONS AGAINST LESSEES FOR USE AND OCCUPATION OF LAND

608 Whenever someone occupies land and it is expressly or impliedly agreed that some rent or other compensation will be payable to the landlord who has permitted that occupation, but no amount has been agreed upon, the landlord may bring an action to recover a reasonable amount for the use of that land by the tenant. There is an implied covenant to pay a reasonable rent arising from the fact that land belonging to the plaintiff has been occupied by the defendant by the plaintiff's permission (*Gibson* v *Kirk* (1841) 1 QB 850). Technically it is an action for damages for breach of the implied covenant.

609 An action for damages for use and occupation is also an alternative means for a landlord to recover payment from a tenant, though it does not often seem to be used in New Zealand, probably because a court would not allow it as a means of claiming, in relation to any period of the term of a lease, any rent in excess of the amount actually agreed upon by the parties to the lease. But when there is doubt about that question or about whether the term has ended, the use of this claim may be advantageous. It "obviates questions about whether the tenancy has come to an end, which could well arise if the terms of the lease are uncertain" (PLERC's *Final Report on Legislation Relating to Landlord and Tenant* (1986) at para 47).

610 In former times in England there were procedural difficulties in recovering rent under a tenancy created otherwise than by a formal lease under seal. The only remedy then available if the tenancy was informal was assumpsit, a form of action on the case for recovery of a reasonable sum for the use and occupation of the premises. The landlord was liable to be non-suited "for a variance" in an action in assumpsit if the evidence disclosed that there had been agreement on a rent (J B Ames at 170). Section 14 of the Distress for Rent Act 1737, which is in force in New Zealand

(Imperial Laws Application Act 1988, First Schedule), was enacted to overcome this difficulty. It enabled a landlord, where the demise was not by deed, to recover "a reasonable satisfaction for the lands, tenements, or hereditaments, held or occupied by the defendant or defendants in an action on the case for the use and occupation of what was so held or enjoyed". The difficulty did not arise when the tenancy was by deed, for then an action to recover rent could be brought in debt (on the covenant), rather than in assumpsit.

611 But, as has been pointed out by the Law Commission in England and Wales in a report on obsolete legislation (Law Com No 179 (1989) at 70), under modern law, whether or not a tenancy is created by deed, it is a question of evidence whether the parties intended that a rent should be payable; and if the court finds that a rent is payable it can award it on the basis of an implied agreement to pay a fair rent or a reasonable rent. The procedural assistance of section 14 is no longer necessary. We believe that it can simply be repealed.

XIX
LONG-TERM DWELLING-HOUSE LEASES

612 There is at the moment a very untidy situation in which the Residential Tenancies Act has for practical purposes largely replaced the sections introduced into the Property Law Act in the 1975 amendment (ie, sections 104A to 104E, 107A, 107B and 116A to 116M). These are all within Part VIII of the Property Law Act and section 142 of the Residential Tenancies Act says that nothing in Part VIII shall apply to any tenancy to which the Residential Tenancies Act applies.

613 The Residential Tenancies Act applies to "every tenancy for residential purposes" (section 4) but excludes a fixed-term tenancy of at least 5 years (section 6). (Other circumstances where that Act does not apply are set out in section 5.)

614 The sections of the 1975 amendment just referred to deal with leases of dwelling-houses and thus with residential tenancies. However, because of the Residential Tenancies Act they have ceased to have application except where a dwelling-house lease is for a fixed term of 5 years or more. That is a relatively uncommon form of lease in New Zealand apart from a leasehold interest used as a form of permanent property ownership, such as a cross lease or a perpetually renewable Glasgow lease, and, as will be mentioned below, these permanent forms are exempt from the application of the 1975 amendment.

615 The primary purpose of the 1975 amendment was to impose minimum requirements for habitability and repair of dwelling-houses. It appears that it was thought when the Residential Tenancies Act was passed that tenants of dwelling-houses for long terms should continue to receive protection of this kind. The sections also give certain rights to a landlord where the tenant fails to meet minimum repair standards; these have also been preserved for long tenancies.

616 Until the Residential Tenancies Act was passed, the landlord and the tenant had the right to refer a dispute to the Rent Appeal Board established under the Rent Appeal Act 1973. Section 104C still refers to the Board but the Rent Appeal Act was repealed by the Residential Tenancies Act.

617 Our impression is that, if the substance of the sections introduced in 1975 should be preserved, their proper place is in the Residential Tenancies Act itself, where they could be placed in a special Part. That is where people searching for the law on leases of residential properties are most likely to look. The Property Law Act is (and should be) a statute of general application. So our proposal is for removal of the repair sections relating to dwelling-houses from Part VIII to a new Part IIA of the Residential Tenancies Act and for two of the sections of Part II of the latter Act

to be made applicable to long-term tenancies: sections 48 (landlord's right of entry) and 62 (abandoned goods). It would remain open to parties to such tenancies, if they wished, to adopt other portions of the Residential Tenancies Act. This is already permitted by section 8 of that Act but it is thought that it is rarely done in practice.

618 Subject to the provisions of the new Part IIA, which would be compulsory, and with one exclusion, the general principles of landlord and tenant to be found in the new Property Law Act would apply to long-term residential tenancies. So would common law rules. Thus they would remain subject to provisions for termination in the event of a breach by the tenant and for relief against termination as found in the new Property Law Act. And that Act's provisions concerning restrictions on assignment or the running of covenants would apply.

619 The one exception would relate to the covenants to be implied by the Property Law Act: see paras 401 to 410. These are not mandatory under our proposals for the Property Law Act (ie, sections to replace sections 106 and 107). They would continue on an optional basis for residential tenancies for a fixed term of 5 years or more (ie, on the basis that the fixed long-term tenancy did not expressly exclude their application). But, because there would be mandatory provisions concerning repair in Part IIA of the Residential Tenancies Act, it would be provided in that Act that the implied covenant to repair on the part of the lessee, which is one of our draft implied covenants (see paras 408 to 410), would not apply.

620 Section 5 of the Residential Tenancies Act contains a large number of exclusions from the jurisdiction of that Act. Section 104A of the Property Law Act presently contains exclusions from the sections introduced in 1975. The list in the Residential Tenancies Act is much more extensive but there seems to be a conflict between the two Acts in two respects only. First, section 104A excludes a lease of land on which a dwelling-house is erected if the lessee is entitled on the termination of the tenancy either to remove it or receive compensation in respect of it. That seems to have been inserted with leases under the Public Bodies Leases Act 1969 of a "Glasgow" lease type in mind (ie, ground leases for 21 years on a perpetually renewable basis), although it could be much better expressed. The exclusion should be carried forward into the new Part IIA but redrafted to clarify any doubt about its effect.

621 The other difference between the statutes is that although both exclude land from which the tenant derives a substantial part of his or her income, the Residential Tenancies Act exclusion operates only where the land is of more than 1 hectare in area and Part VIII where it is 1.25 hectares or more. This is an odd (and probably unintended) anomaly. For future leases of 5 years or more it is suggested that the 1 hectare measure be used, which would require no more than dropping the Part VIII exemption.

622 The repair provisions in sections 116D to 116K, which in substance could be transferred to Part IIA, are drafted in a rather fussy style and could be simplified. In a lease covered by the 1975 Amendment the tenant is (in essence) to keep the dwelling-house in clean condition and to make good damage caused by the wilful or negligent act or omission of the tenant or someone allowed by the tenant to enter or remain in the premises, but there is no liability for fair wear and tear. On the other hand, the landlord, under section 116H, warrants that the premises are and will remain in a fit and habitable condition for residential purposes but this obligation does not limit the tenant's obligations to repair. The landlord's warranty might not apply at common law except on a letting of furnished premises.

623 We have suggested (para 408) as one of the general implied covenants, which would (unless excluded) be in every lease of land other than a lease for one year or less, a covenant by the lessee to keep and deliver up the premises in "the same standard of repair and condition as they were at the commencement of the term" with exclusions for perils and for reasonable wear and tear. This obligation under the proposed new Property Law Act would be less onerous than the implied repair covenant in the present Property Law Act in that the tenant is not responsible for putting the premises in good condition and merely has to ensure that they do not deteriorate beyond reasonable wear and tear. On the other hand, the 1975 Amendment Act requirement is for repair only where there is "damage" from a wilful act or from negligence. Moreover, the landlord is obliged to provide the premises in a state fit for occupation as a residence. So the dwelling-house tenant's position is a little better under the 1975 provisions. For this reason it seems appropriate to bring the substance of them forward into the new Part IIA and to exclude the implied covenant for repair (ie, confine it to a commercial or farming context) because it would be inconsistent with the compulsory provisions of Part IIA. (See also our suggestions regarding the covenants implied by sections 106 and 107 of the Property Law Act at paras 399-410.)

624 An alternative to these relatively complicated changes might be simply to repeal section 6 of the Residential Tenancies Act and so bring long residential tenancies within the regime in that Act. If this were done it would be very important to ensure that "Glasgow" leases were effectively exempted (see para 620).

Questions:

Q152 Should the 1975 amendments relating to long residential tenancies be retained?

Q153 Alternatively, should section 6 of the Residential Tenancies Act 1986 be repealed?

PART E: MISCELLANEOUS

XX
EASEMENTS, COVENANTS, ENCROACHMENTS, LANDLOCKED LAND, TREES AND STRUCTURES

625 Most of the sections in Part IX are of fairly recent origin and, judging by reported caselaw, do not appear to have thrown up any significant drafting problems or require changes in their substance. This is also true of section 122 (easements in gross), though it is of remoter origin, and of sections 123-125 (light and air easements) which, though in the Act since 1927 in their present form, have only recently been the subject of their first reported decision: *Henderson* v *Knowles* (1991) 1 NZ ConvC 190,704, which contains nothing suggesting need for any substantive amendment, although the drafting style of the sections should be modernised.

626 Sections 126 to 126G follow from a report and draft statute prepared by PLERC in *Report on Positive Covenants Affecting Land* (1985) and were enacted in 1986. There may be a case for moving section 126A into the Land Transfer Act. It gives the District Land Registrar the power to register a notification of a covenant which then "shall be an interest within the meaning of section 62 of the Land Transfer Act 1952". However, a notification does not give the covenant "any greater operation than it has under the instrument creating it".

AUTHORISED ENTRY

627 Section 128 allows a District Court to authorise a landowner to enter on adjoining land for the purpose of erecting, repairing, adding to or painting a building, wall, fence or other structure on the applicant's land. There has been no reported case which considers this section. The following matters could be considered in redrafting:

- The form of order which the court may make could be more explicit: an order authorising the applicant or any contractor or other agent engaged or employed by the applicant to do the various works.

- It could be made clear that, provided there is appropriate authorisation in the court order, the entry by the applicant can be with plant, machinery, vehicles, equipment and materials. Perhaps the court should be empowered to enable the applicant temporarily to store materials on the land.

- The court could be given power to delimit the period of time for the work and the hours of work.

- The applicant could be required to give the adjoining landowner and any person in possession of the adjoining land at least 10 working days'

notice of the intention to make application to the court. In many cases this may bring matters to a head and enable a satisfactory settlement to be negotiated without need for court proceedings.

- There may be advantage in giving power to make application to a contractor or agent engaged or employed by a landowner, although usually the landowner will co-operate by making the application on behalf of the contractor.

BUILDINGS ON WRONG LAND

628 Section 129 deals with a building which straddles a boundary while section 129A deals with one which is entirely on the "wrong" land. It does not appear that under section 129A the land, which is called in the section "the original piece of land", has to be adjacent to the land called "the piece of land wrongly built upon".

629 The authority for the proposition that section 129A applies only where the building is entirely on the piece of land wrongly built upon is the judgment of Hardie Boys J in *Blackburn* v *Gemmell* (1981) 1 NZCPR 389, 392-3. In an unreported judgment in *Norris* v *Weal*, noted at [1985] BCL 51, Gallen J came to the opposite conclusion. There could be some merit in inserting the word "entirely" after the word "building" the first time it appears in section 129A(1). This would guide legal advisers to the correct section by making it clear that section 129A does not deal with an encroachment (ie, a straddling situation).

630 One other possible approach would be to dispense with section 129 altogether on the basis that section 129A be amended so as to cover a situation of straddling. However, it is drafted with one clear time sequence in mind, namely that the problem arises because a building is erected in the wrong place in relation to an existing boundary. While section 129 contemplates this sequence, it also assists where the building has first been erected and then, afterwards, there has been a subdivision which somehow contrives to put a boundary line through the middle of the building. Perhaps with modern surveying methods and subdivisional controls this is now less likely to occur, but it cannot be ruled out in the case of buildings erected and subdivisions carried out many years ago. The safest course therefore seems to be to preserve both sections, while at the same time making it clear that one applies in the case of encroachments and the other in the case of a building which is entirely on the wrong land.

631 In each case the definition of "building" should, we think, be expanded to include any structure and, particularly, paths, driveways and retaining walls. It is not envisaged that a boundary fence should be covered as this can be dealt with under fencing legislation.

632 In *Blackburn* v *Gemmell* it was pointed out that under section 129A there was provision for the vesting of a curtilage around the offending building but no such provision appears in section 129. It could usefully be added to section 129.

LANDLOCKED LAND

633 Section 129B dealing with landlocked land was enacted in 1975. There has been quite a large number of cases on it but none of them has demonstrated any problems of interpretation nor produced a result which seems out of keeping with the spirit of the section. The section itself has been described as "very comprehensive and very carefully drawn" (*Murray* v *Devonport Borough Council* [1980] 2 NZLR 572, 573, Speight J).

634 In *Roberts* v *Cleveland*, unreported, High Court, Nelson, 30 March 1988, M 18/87 (noted 5 BCB 7), subsection (3)(a) was found to be mandatory. The court should be given dispensing power where there is no good purpose in requiring every adjoining owner to be served.

TREES AND STRUCTURES

635 Section 129C confers the right to apply to a District Court for an order for the removal of trees and structures on neighbouring land. It is also drawn with considerable detail and care. The orders which may be made under this section are limited to situations in which there is:

- danger to life or health or to property;
- obstruction of a view; or
- other "undue interference" with the reasonable enjoyment of the applicant's land for residential purposes.

636 Section 129C applies only to residential land although it is clear from subsection (3) that an application can be made if the applicant's land is used for residential purposes regardless of whether the land of the defendant is land to which this section applies. Formerly section 26A of the Fencing Act 1908 forbad the planting of gorse or trees on or alongside boundaries or fences without consent of the neighbour and gave the neighbour a right of entry to remove any planted in breach of the section. Section 26A was not restricted to residential properties. When section 129C was enacted, farm land (except where it was adjacent to residential land) was deliberately excluded from the ambit of the new section. This was done to safeguard property owners in farming areas who might otherwise be concerned about their shelter-belts and plantations. Their trees were not to be affected unless they were adjacent to a house used for residential purposes.

637 However, representations made to the Justice Department, particularly on the part of Federated Farmers and the New Zealand Local Government Association suggest that problems caused by trees and shelter-belts in rural areas are both common and serious. Among those matters complained of are:

- root systems affecting growth and yields on adjacent fields and clogging drains;
- nuisance caused by branch and leaf falls; and
- shade affecting crops.

638 The Commission would be interested in hearing from those who have views for and against the extension of section 129C to land used for agricultural or horticultural purposes. If the Commission were to recommend such an extension it would do so on the basis that the balance achieved by the careful drafting of the present section is preserved. The Commission is conscious that an amendment along these lines will raise issues of competing land use, but it is inclined to think that the section gives the court sufficient guidance in determining such issues.

639 It could, however, be made clearer (both in relation to domestic and rural properties) than an order could be made where there are serious adverse effects on drains or caused by leaf falls. It would also, we think, be helpful to provide in the section that the court is empowered to order the defendant to pay compensation for any damage caused to the property of the applicant in the course of the process of trimming or removal of trees. It might also avoid the need for repetitive applications under the section if the court were more plainly empowered to make orders as to the future; for example, that a particular tree or a shelter-belt is at all times to be kept within certain dimensions or that clearance of drains from roots or other material emanating from a tree or shelter-belt is to occur with specified regularity.

MAORI LAND

640 As sections 129B and 129C apply to Maori land, the Law Commission thinks that it may be desirable to have in each an express requirement that Maori cultural values be taken into account by the court in exercising its discretion thereunder.

Questions:

Q154 Should section 128 be redrafted as suggested in para 627?

Q155 Should section 129C be extended to agricultural and horticultural land?

Q156 Should section 129C be amended as suggested in para 639?

XXI
MARRIAGE SETTLEMENTS

641 Part XI of the Act comprises sections 131 and 132, which vest in the trustee or trustees of marriage settlements powers to lease or sell real property comprised in the settlement. The sections were carried over from the 1908 Act. They are the only sections in the Act expressly to vest powers in trustees. (The Trustee Act 1956 contains the statutory powers vested in trustees generally.)

642 A marriage settlement is "a settlement of money or property in trust for one or both spouses and/or their issue in consideration of the parties marrying each other" (Fisher at para 1.17). A marriage settlement is indistinguishable from other settlements of land governed by the Trustee Act 1956 because in both cases a life interest in land may be created. The only relevant distinction is that in the case of a marriage settlement, the consideration is the marriage of the parties to each other.

643 Fisher's discussion of marriage settlements concludes (para 1.18) with the observation that the structure is now one little used in practice although it has a potential usefulness; the structure could be used to avoid the division of gifted property under the Matrimonial Property Act 1976. However, that observation is followed by his comment that agreements contracting out of the provisions of the Matrimonial Property Act (section 21 agreements) may perform the same function.

THE TRUSTEE ACT 1956

644 The power to lease conferred upon trustees of marriage settlements by section 131 of the Property Law Act (which, as will be seen, is not quite the same as the power to lease vested in trustees by the Trustee Act) appears to prevail over the power to lease in the Trustee Act. Likewise, the differently worded power to sell in section 14 of the Trustee Act would seem to be, for trustees of marriage settlements, subordinate to the power to sell in the Property Law Act. However, the Trustee Act arguably confers powers upon trustees of marriage settlements, in the absence of any express reference in the Trustee Act to the contrary, additional to those conferred by sections 131 and 132.

645 The section directly analogous with section 131 (the power to lease) is 14(1)(e) of the Trustee Act. The similarities between the two sections are these:

- both sections refer to a power to lease *all or part* of the settled land; and
- both sections restrict the term of the lease to a maximum of 21 years.

646 The differences between the sections are these:

- The lease takes effect in possession within *one year of the date of the grant* in section 14(1)(e), and within *six months from the making of the lease* in section 131.

- The rent must be *reasonable* under section 14(1)(e) and a *reasonable yearly rent* in section 131.

- The trustees, under section 131, *are prohibited* from taking a fine or premium for the making of the lease, but under section 14(1)(e) *may* levy a fine, premium or foregift. Any levy under section 14(1)(e) is deemed part of the rent and the trustee must account to the beneficiaries under the trust.

- Section 131 expressly requires the lessee to enter into a counterpart, but there is no equivalent provision in the Trustee Act 1956.

- Additional provisions, expanding upon the trustees' power to lease, are contained in sections 14(1)(d), 14(1)(f), 14(5)(a), 14(5)(b), 14(5)(c) and 14(6). Those powers may also be enjoyed by trustees of marriage settlements.

647 Section 14(1) of the Trustee Act contains a power to sell land analogous to the trustees' power to sell in section 132. The differences are these:

- The trustees' power to sell in section 132 arises either, if there is no life tenant, at their own discretion, or following a written request from the life tenant in possession (or a guardian or manager). The Trustee Act does not specify any such preconditions, the power being conferred on trustees outright.

- In both cases the trustees can not only sell but also exchange the land. In section 132 the exchange must be for land of like nature or tenure in New Zealand. In section 14(1) the exchange must be for land of a like nature and a like *or better* tenure.

- The trustees are, under section 132(2), given directions to apply the sale proceeds of other land of like nature or tenure in New Zealand. If land is purchased, it is subject to the terms of the settlement. No equivalent direction is given to trustees in the Trustee Act.

- Under section 132, until the sale proceeds are applied in the purchase of substitute land, they

must be invested in authorised investments (which introduces, by implication, the investment provisions of the Trustee Act). There is no equivalent provision in the Trustee Act, although it is implicit that any investment of sale proceeds must comply with that Act.

- The Trustee Act contains provisions additional to those contained in section 132 regarding the sale or disposition of land: see sections 14(1)(c), 14(2), 14(4), 14(6), 16 and 17.

- In section 132, trustees may, in a partition of land, give or take any *money* by way of equality of exchange or partition, and in section 14(1)(b), the trustee may give or take any *property* by way of equality of exchange or partition.

648 This examination shows that although there are differences of detail between these powers conferred by sections 131 and 132 and those conferred by the Trustee Act, there is broad similarity. It is unclear how the sections 131 and 132 powers are intended to operate alongside the wider powers in the Trustee Act, in the absence of any statutory direction. (There seems to have been no judicial consideration of the question.)

649 The Law Commission has concluded that there is no longer good reason for retaining a Part of the Property Law Act for marriage settlements and that sections 131 and 132 should be absorbed into the Trustee Act. The powers to sell and lease land in the Trustee Act should apply to trustees of marriage settlements. However, it should be made clear that trustees may sell land subject to marriage settlements only if there is no life tenant or following the written request of the life tenant in possession. In this way the only significant difference between the powers conferred by the two Acts would be preserved.

Question:

Q157 Should sections 131 and 132 be absorbed into the Trustee Act in the manner suggested in para 649?

XXII
SERVICE OF NOTICES

650 Section 152 is an important section governing the manner in which notices required or authorised under the Act are to be served. It was amended in 1982, that amendment having given rise to some controversy at the time and to some reported caselaw.

WHEN SECTION IS MANDATORY

651 Notices under sections 92 or 118 must be served in accordance with section 152 (by personal delivery or registered letter): see subsection (6A). The section applies to other notices only in so far as a contrary intention is not expressed in any instrument. The Commission wonders why a notice under section 90 is exempt from the mandatory method of service. If, as we believe, section 152(6A) should remain, it ought also to extend to notices under section 90. It should also continue to apply to notices to purchasers in possession.

METHOD OF SERVICE

652 The provision under which a notice sent by registered letter is deemed to have been served when in the ordinary course of post it would have been delivered was in 1982 qualified by words which enable the intended recipient of the notice to prove that, otherwise than through any fault on the intended recipient's part, the notice was not delivered at that time. In this case it is *not* deemed to have been delivered in the ordinary course of post.

653 In *Matich* v *United Building Society* [1987] 2 NZLR 513 it was said that neither actual delivery to nor actual receipt by the mortgagor is required for effective service by registered mail under the section. The section, by a fiction, declares service to have been effected at a certain time. But that presumption, since the amendment in 1982, can be rebutted by proof that the registered letter was not in fact delivered at the time when in the ordinary course of post it would have been.

654 "Delivery" means actual delivery either to the addressee or an agent (actual or ostensible): see *Matich* v *United Building Society*. There is no room for importing into the term some form of constructive delivery. Nevertheless it seems to be the law that if the notice giver can show that by some means the person to whom notice is sought to be given has come into actual possession of the notice document, service is achieved within the section. In *Woods* v *Tomlinson* [1964] NZLR 399 it was sufficient that a notice sent by ordinary post to the solicitors acting for the plaintiff had been brought to his attention by the solicitors. This was held to be personal delivery within section 152. The Commission suggests that this view be confirmed: a statement in the new section that a notice is sufficiently served if actually received by the person to whom it is directed (or an agent who has actual or ostensible authority to receive it), however this occurs.

655 Henry J acknowledged in *Matich* that the construction which he placed on section 152 could cause practical problems for a mortgagee desiring to effect service by registered post in that unless the "advice of delivery" (AR card) procedure is used the actual date of service may be uncertain. He noted that the court could still give directions as to the manner of service under section 152(4) in cases of doubt. In *Cook* v *United Building Society* [1987] 2 NZLR 519 Barker J followed this judgment and commented:

> ... there can be no great hardship for the mortgagee to obtain a process server to effect personal service of the notice: if there is a suggestion of a mortgagor evading service, then it is possible to obtain an order of the Court in the nature of substituted service under section 152(4). (at 524)

656 Since the decisions in *Matich* and *Cook* the practice of conveyancers and financiers in relation to service under section 152 has changed. The most commonly used method of service is personal service. In some cases registered mail is used but only, it appears, the variety of registered mail that involves the obtaining of the signature of the addressee (or someone apparently authorised by the addressee) by way of acknowledgment of receipt. (The term "registered letter", as used in the section, no longer has any official status, for the postal regulations in which it appeared have been repealed as part of the process of corporatisation of the Post Office as NZ Post Ltd.)

657 Ordinary registered mail, ie, without acknowledgment of receipt, is evidently not much used. It is (correctly, we think) regarded as being risky. Few people now rely upon the "ordinary course of post", as those words are used in section 152(1), since the additional words added in 1982 make it all too easy for a supposed recipient to claim that delivery did not occur at all in the ordinary course.

658 It seems to the Commission that for the protection of mortgagors, lessees and purchasers in possession the new section (replacing section 152) should require service *either* by personal delivery *or* by a delivery service (NZ Post, courier or some equivalent). In the latter case it should be required that the person providing the delivery service is independent and obtains a written acknowledgment from the recipient. We call this "acknowledged delivery". The reference to ordinary course of post can simply be dropped. Service would not be complete until it actually occurs, as evidenced, in the case of service by delivery service, by a signed acknowledgment.

659 Clause 169(1) of the Companies Bill which is now before Parliament contains rules for service of notices on companies. The section sets out a sequence in which attempts to serve a company must be made. The Commission thinks that the methods of service available under that Bill should be available under the Property Law Act, which could be achieved

by providing in the proposed new Property Law Act that service in accordance with section 169(1) constitutes personal service on a company for the purposes of the Property Law Act. In addition service could be made by acknowledged delivery.

660 In *Matich* Henry J said that delivery meant actual delivery or "handing over of the letter either to the addressee or to his agent (actual or ostensible)". The law enables service upon someone who appears to have authority to accept the notice on behalf of the addressee. The risk of relying on ostensible authority, if service were challenged, would seem to fall on the person giving the notice. This position should, we think, be preserved: it should be stated that it is sufficient that the notice is served by acknowledged delivery signed for by someone with actual or ostensible authority from the addressee.

FORM OF SECTION 92 NOTICE

661 The difficulty created for mortgagees by the 1982 amendment is compounded by the fact that section 92 presently requires that a notice under that section nominate the date on which power of sale can be exercised and moneys called up. The Law Commission has suggested above (para 295) that the obligation to name a particular date in a section 92 notice be done away with and replaced by an obligation to include in the notice a statement that power of sale and entry into possession will be exercisable, and that the mortgage moneys can be called up, 20 working days after the date of service of the notice if the specified default is not remedied. This assumes that the mortgagor will be aware of the date of service, as should be the case if the methods of service are restricted as outlined in paras 658 and 659. The change should not disadvantage a mortgagor who has been properly served. It will avoid for the mortgagee the need to change the date in the notice if service is delayed.

SERVICE OVERSEAS

662 The Commission sees no need to restrict service (either personal or by acknowledged delivery) to service in New Zealand. It should be possible to effect service overseas without need for a court order. No question of jurisdiction arises: the notice is not a court proceeding, merely a warning of future action.

JURISDICTION FOR SUBSTITUTED SERVICE

663 In section 152(6), reference to the "Court" is restricted to the High Court where the notice relates to a sum of money exceeding $40,000. However, the court's role under this section is simply the making of an order relating to the manner of service of a notice where difficulties are encountered. The whole of this jurisdiction should be vested in the District Courts, with consequent savings of time and money, particularly where the mortgagee's solicitor is in a place remote from a High Court Registry.

SERVICE ON CROWN

664 If the proposed new Act is to bind the Crown, as the Law Commission thinks it should, some provision needs to be made for service on the Crown. Perhaps the best solution is to require that any notice under the Act be served on the chief executive (or a delegate) at the head office of the relevant department - either personally or by delivery service.

DISSOLVED COMPANIES ETC

665 Where the party to be served is a company which has been dissolved or where the property concerned has been disclaimed, we suggest that service should be on the Secretary for the Treasury. Where the party to be served is bankrupt, service should be on the Official Assignee.

Questions:

Q158 Should a notice under section 90 be required to be served in terms of the new section which replaces section 152?

Q159 Should a notice be sufficiently served if actually received by the addressee or that person's actual or ostensible agent?

Q160 Should service under the section be required to be either:

- personal, or
- by acknowledged delivery - with written receipt signed by the addressee or that person's actual or ostensible agent?

Q161 Should service be permitted by these means outside New Zealand without need for a court order?

Q162 Should jurisdiction to order substituted service be vested exclusively in the District Courts?

Q163 How should the following be served:

- the Crown?
- a dissolved company?
- the owner of disclaimed property?
- a bankrupt?

XXIII
RIGHT TO HAVE INSURANCE PROCEEDS APPLIED IN REINSTATEMENT

666 Section 83 of the Fires Prevention (Metropolis) Act 1774 remains part of New Zealand law: Imperial Laws Application Act 1988, First Schedule. It was originally passed as a deterrent to arson. It gives an insurance company the right to insist upon applying the insurance moneys in reinstatement of destruction of or damage to buildings caused by fire. It also gives a person with an interest in the property less than full ownership ("a person interested") the right to require the insurance company so to apply the insurance moneys. Contracting out of the section is permissible (*Reynard* v *Arnold* (1875) 10 Ch App 386 and *Searl* v *South British Insurance Co* [1916] NZLR 137).

667 Section 83 gives no right to the owner/mortgagor of the property to insist that the money be used for reinstatement (*Reynolds* v *Phoenix Assurance Co Ltd* [1978] 2 Lloyd's Rep 440, 462). A "person interested" is therefore a mortgagee, a purchaser or a tenant of the property.

668 A *mortgagee* of land usually has by contract with the mortgagor the right to elect whether to have the insurance proceeds paid to it or to have them applied in reinstatement: see clause (6) of the Fourth Schedule to the Act. Subject to the point about to be made, it would therefore only be in the rare circumstance where a clause of this kind was not contained or implied in the mortgage that a mortgagee would depend upon section 83.

669 The provision has some residual value for a mortgagee only if by mischance its interest as mortgagee has not been noted on the insurance policy and is not recognised by the insurer. But where there is more than one mortgage the right to require reinstatement should be vested only in the first mortgagee, which should not be susceptible of having its wishes overridden by a subsequent mortgagee.

670 Section 13 of the Insurance Law Reform Act 1985 gives a *purchaser* of the land the benefit of the vendor's insurance policy until the purchaser takes possession of the property but, apparently, only to the extent of the right of the vendor to be "indemnified" by the insurer. Section 13 could be extended so as to give the purchaser the right to have the property reinstated by the insurer where the vendor has that right under the insurance policy.

671 If an amendment to this effect is made to section 13, re-enactment of section 83 will be of limited use to a purchaser. It will give a purchaser some protection after taking legal possession of the property if the purchaser has failed to arrange its own insurance cover.

672 One New Zealand case has determined that a purchaser holding under a conditional contract is not a person interested for the purposes of section 83 (*Moreton* v *Montrose Ltd* (unreported, High Court, Auckland, 6 August 1984, A 967/81, Henry J)). The Commission suggests that this decision should be reversed by the new section. It now seems clear that a conditional purchaser has an interest in the land, and is entitled to protect it by caveat (*Kuper* v *Keywest Constructions Pty Ltd* (1991) ANZ ConvR 115). If section 83 is to be re-enacted, a conditional purchaser should therefore be a person interested for insurance purposes.

673 The third of the classes of interested persons is that of *tenants*. Usually the lease is brought to an end by the event of destruction or damage of the premises, but, if it is not, a tenant may find it valuable to have the right to call for reinstatement. However, any new section replacing section 83 would have to take account of the fact that the tenant might have a lease of part only of the landlord's building. It does not seem fair that a tenant of part of the building should have the right to call for insurance moneys to be applied in reinstatement of the entire building or, in some circumstances, even of that part.

674 If the section were to be extended to cover a conditional purchaser, it is possible that a notice might be given and then, afterwards, the purchaser's interest in the property might lapse because the condition is not satisfied. Similarly, a tenant may give a notice before the landlord elects to terminate the lease under a power given in the lease agreement. A section giving rights to such persons would have to contain a provision protecting an insurance company which continues to act on such a notice and also protecting the owner from a decision by the insurance company to withdraw from reinstatement when the process is part completed. This could be handled by providing that an insurance company must act on a notice given by a person with a defeasible interest; but if the notice giver's interest later ceases and that fact is made known to the insurance company before it becomes committed to the reinstatement work, the insurance company could elect not to proceed. However, an act of defeasance after the insurer becomes committed would not entitle the insurance company simply to pay the insurance proceeds, or the balance of them, to the owner unless the owner, the insurer and any other person interested are all agreeable, for that might leave the work partly completed.

675 It is clear from this discussion of the manner in which a re-enactment of section 83 could be stated, that the conferment of rights on each class of "person interested" creates complication. Will those persons receive benefits which justify retention of a version of the section? We think that this is doubtful; certainly, in few of the decided cases has a person interested been helped by the section. The benefits for all classes will occur in situations which arise fairly infrequently, and then only when the person concerned has failed to arrange his or her own insurance cover. We have

the impression from our discussions with persons in the insurance industry that insurers may prefer to rely upon rights given to them under the policies of insurance to apply insurance moneys in reinstatement, rather than upon a statutory right.

676 A further difficulty relates to damage caused by fire resulting from an earthquake, which is regarded as earthquake damage, not fire damage. The section should not apply to it. We say this because we are aware that many building owners have indemnity cover only against earthquake and resultant fire. It is considered too expensive to have reinstatement insurance for these risks. It would therefore be unreasonable to give to persons interested the right to require reinstatement in these circumstances.

677 On balance, the Commission provisionally thinks that it may be best simply to repeal section 83, but at the same time to extend section 13 of the Insurance Law Reform Act as described in para 670.

Questions:

Q163 Should section 83 of the Fires Prevention (Metropolis) Act be re-enacted?

Q164 If so, should "person interested" be defined to include a first mortgagee, a purchaser and a lessee and should the possibility of cessation of a defeasible interest be provided for as suggested in para 674?

Q165 Should section 13 of the Insurance Law Reform Act 1985 be extended as suggested in para 670?

GLOSSARY

adverse possession	occupation of land in a manner inconsistent with the right of the true owner.
attornment	the (express or implied) agreement of a lessee to become the tenant of the owner of the reversion (qv), the lessor.
contingent condition	"a provision that on the happening of some uncertain event an obligation shall come into force or that an obligation shall not come into force until such an event happens" (Volume I, *Chitty on Contracts* (26th ed) Sweet & Maxwell, London, 1989 at para 795). An example is a finance condition in an agreement for sale and purchase of land.
corporation aggregate	a group of persons who are incorporated as one corporation (eg, a company with two or more shareholders).
covenant	originally the term was used to describe an undertaking made in a deed; now, however, the term includes promises in informal documents.
disclaimer	the act of renouncing a right to property or other claim.
distress for rent	a remedy whereby a landlord may seize the chattels of the tenant and sell them as a means of recovering arrears of rent.
doctrine of lost modern grant	a doctrine whereby a right in respect of land enjoyed for a long period was justified by the fiction that it must have been created by a deed of grant now lost.
easement	a right attaching to one piece of land entitling the owner to exercise it over land owned by someone else (eg, a right of way enjoyed over neighbouring land).

encumbrance	a claim or liability attaching to property, including a mortgage or charge.
escrow	where an instrument (qv) evidencing obligations between two or more parties is held on their behalf on condition that the holder shall deliver it on the happening of a stated condition, and it shall then take effect as a deed.
estoppel	a situation in which one party has made a representation by words or conduct upon which another has relied and the first party is unable to deny the state of affairs thus represented.
indenting	the former practice whereby a deed was made in two parts written on one sheet and then divided by an indented or jagged line so that each could fit the other and so be identified as genuine. The deed was called an indenture.
instrument	a document in writing which either creates or affects legal or equitable rights or liabilities.
partition	the division of land held in co-ownership into parts to be held by the former co-owners separately.
possessory interest	a right to land by virtue of possessory title (qv).
possessory title	a title to land acquired by occupying it for a certain period of time without paying rent or otherwise acknowledging the title of the former owner.
prescriptive right	a right held under prescriptive title (qv).
prescriptive title	a title created by enjoyment of a right (eg, a right of way) against the owner of land for a period of such duration as to establish the right.
profit à prendre	a right to enter land and take from it some profit of the soil (eg, timber) or part of the soil itself (eg, minerals).

remainder	an estate in land which takes effect in possession on the determination of all preceding estates.
reversion	the interest in land held by an owner of an estate who has granted out of it a lesser estate (eg, a lease) but has not disposed of the whole estate. A reversion is usually transferable.
seisin	"Seisin denoted a particular kind of possession" (Hinde McMorland & Sim, at para 4.003). Thus (quoting from Megarry and Wade at 48) "a person was seised if - (i) he held an estate of freehold, (ii) in land of freehold tenure, and (iii) either he had physical possession of the land, or a leaseholder...held the land from him."
severance of reversion	when a reversion is subdivided or partitioned so as to be in separate ownerships.
subrogation	the principle that a person who discharges a liability for which someone else is primarily liable is put in the place of that other person for the purpose of obtaining relief against a third party. Thus an insurer is entitled to stand in the place of an insured party and to exercise all the insured's rights to recover from any person who caused the loss in respect of which the insured claimed under the policy of insurance.
succession interest	a right to property arising by reason of the death of the person entitled to that property.
thing (or chose) in action	"...choses in action comprise all property rights of which it is impossible to take physical possession..." (Sykes at 691). It is most commonly used in relation to debts, which can be sued for in an action.

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