

DFC Financial Services Limited

*Appellants*

v.

- (1) Martin Leo Coffey
- (2) Frederick Herbert Morris and
- (3) Peter Martyn Roberts

*Respondents*

FROM

THE COURT OF APPEAL OF NEW ZEALAND

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JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE  
OF THE PRIVY COUNCIL, DELIVERED THE  
18TH MARCH 1991  
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*Present at the hearing:-*

LORD KEITH OF KINKEL  
LORD ACKNER  
LORD OLIVER OF AYLINGTON  
LORD GOFF OF CHIEVELEY  
LORD JAUNCEY OF TULLICHETTLE

*[Delivered by Lord Goff of Chieveley]*

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There is before their Lordships an appeal by the appellants, DFC Financial Services Limited ("DFC"), from a decision of the Court of Appeal of New Zealand, whereby the court allowed an appeal by the three respondents from a decision of Master Hansen pursuant to which summary judgment was entered in favour of DFC against the three respondents in two sums of NZ\$10,319,455.73 and NZ\$2,058,000 respectively, plus interest.

The dispute in the present case has arisen from financial difficulties of the Kearns group of companies. A company called Brookstock No. 17 Limited ("Brookstock") was a subsidiary of the Kearns Corporation Limited ("Kearns") until January 1988, when 99 of its 100 shares were transferred to the Prudential Building Investments Society of Canterbury Limited ("Prudential"), Prudential being a company managed by Kearns. The three respondents were senior executives in the group, Mr. Coffey being the Chairman of Kearns and a Director of Brookstock, Mr. Morris a Director of Kearns and an Executive Director of Brookstock, and Mr. Roberts Chief Executive Officer of Kearns and a Director of Prudential. Before the financial difficulties arose, there were numerous

dealings between DFC and companies in the Kearns group; and a method of financing was agreed upon under which companies in the group would lend money on first mortgages, and obtain finance for these operations from DFC against those securities. Brookstock was formed with the object of acquiring first mortgage securities from the lending companies, with the intention of borrowing money from DFC on the security of the mortgages. In due course Brookstock entered into an agreement with DFC dated 10th June 1987 ("the first agreement"), under which DFC agreed to make available to Brookstock a loan facility of NZ\$10 million. In the agreement, Kearns and the three respondents were named as guarantors of the obligations of Brookstock. On 30th June 1987 Brookstock as borrower, and Kearns and the three respondents as guarantors, entered into a deed of debenture ("the debenture") securing all advances to Brookstock and obligations of Brookstock to DFC. Thereafter, on various dates in 1987, Brookstock drew on the full amount of the facility made available to it under the first agreement.

Under a further agreement dated 4th August 1988 ("the second agreement") DFC agreed to make available to Brookstock a further loan facility of NZ\$2 million. Once again, Kearns and the other three respondents were named as guarantors of the obligations of Brookstock. On 12th August 1988, Brookstock drew on the full amount of the facility so made available to it. The advance so made constituted a further advance under the debenture, which accordingly applied to it.

It appears that, following an inspection by the New Zealand Department of Justice in the autumn of 1988, it came to light that many mortgages acquired by Brookstock had not been transferred to it. As a result, Brookstock was in breach of its obligations to DFC under the two agreements. Mr. Roberts, as Chief Executive of Kearns, gave instructions for assignments to be prepared; but the Chief Executive of Kearns, a Mr. Reid, refused to sign transfers from Prudential to Brookstock. On 20th February 1989 DFC, having carried out an examination of Brookstock's records, faxed a letter of complaint to Brookstock. In the event two deeds of assignment from Prudential to Brookstock were executed on 23rd February 1989. However on the day of their execution, a petition to wind-up Prudential was filed in the High Court, and provisional liquidators were appointed; and on the following day DFC appointed receivers and managers of Brookstock. On 28th February 1989, DFC served on the three respondents as guarantors demands for payment of the principal and interest secured under the debenture, viz. \$12,377,455.73, (being the total of the two sums payable under the two agreements). This sum remained unpaid, and on 19th April 1989 DFC commenced proceedings against the three respondents, claiming two sums as due

under the guarantees, viz. \$10,319,455.73 in respect of principal and interest (to 27th February 1989) in respect of the first agreement, and \$2,058,000 in respect of the second agreement. DFC sought summary judgment against the three respondents; and on 19th October 1989, following a hearing before Master Hansen, summary judgment was entered against them for the sums claimed plus interest. A stay of execution having been granted upon terms, the three respondents appealed to the Court of Appeal against the decision of Master Hansen; and on 19th July 1990 the Court of Appeal allowed the appeal, the judgment of the court being delivered by Somers J.

Before Master Hansen, numerous points were advanced on behalf of the three respondents in opposition to DFC's application for summary judgment. One of these points was that, under the terms of the debenture, no sums were payable by the respondents under their guarantees unless a demand had first been made on Brookstock, and no such demand was made. All these points were rejected by Master Hansen. The Court of Appeal however accepted the respondents' argument that a demand on Brookstock was a necessary condition of their liability, and on that ground alone the Court of Appeal allowed the appeal, without referring to any of the other issues which had been canvassed before them, as they had been before the Master. It is against that decision that DFC now appeal to their Lordships.

The resolution of this issue turns upon the proper construction of the relevant terms of the debenture. The following provisions are relevant:-

1.02 (Repayment of Principal)

"The Borrower will pay to DFC on demand all amounts of Principal together with interest to the date of payment or repayment at such rate as may from time to time be charged by DFC under the terms of the relevant Loan Agreement pursuant to each and every Facility and together with any expenses costs and other charges incurred by DFC in preparation or enforcement of this debenture or any collateral security or any guarantee agreement or any other documentation on a full and unqualified indemnity basis PROVIDED HOWEVER DFC shall not have the right to make demand under this debenture for all such moneys other than those due and payable in terms of the relevant Loan Agreement unless and until:

- (a) the Borrower fails to pay DFC on due date or when otherwise payable any sum of money due and payable by the Borrower to DFC in respect of any Facility; or
- (b) the occurrence of any event of default listed in clause 5.03."

5.01 (Crystallisation of charge)

"Upon the occurrence of any one or more of the events listed in clause 5.03 all moneys hereby secured shall become immediately due and payable without the necessity for any notice of default or further demand by DFC and this security shall attach and become fixed as regards all the assets property and undertaking both present and future charged by this debenture."

5.02 (Rights may be exercised at any time after default)

"Notwithstanding any delay or previous waiver DFC may compel payment of any moneys due and payable in terms of clause 5.01 at any time following the occurrence of an event of default specified in clause 5.03 by pursuing any of the rights powers and remedies conferred upon it by this debenture or by any other security or agreement or at law."

5.03 (Events of default)

This clause specifies 18 separate events of default, including

- "(a) if the Borrower defaults in the performance or observance of any of the provisions of any covenant condition arrangement or agreement between the Borrower and DFC;
- (j) if the Borrower stops trading or if in the opinion of DFC the Borrower ceases to carry on its business or any substantial part thereof or threatens to cease the same;"

Clause 8 is concerned with Guarantee and Indemnity.

Clause 8.01 provides:-

"The Guarantor in consideration of DFC agreeing to make each Facility available to the Borrower hereby unconditionally and irrevocably as principal obligor and not merely as surety guarantees to DFC:

- (a) full and prompt and complete performance by the Borrower of all its obligations under any Loan Agreement between DFC and the Borrower existing from time to time; and
- (b) the due and punctual payment of all sums payable now or in future to DFC by the Borrower under any Loan Agreement when and as the same shall become due (whether at maturity, by acceleration or otherwise)

and undertakes with DFC that if and each time that the Borrower shall be in default in the payment of any sum whatsoever under any Loan Agreement the Guarantor will forthwith make good the default and

unconditionally pay to DFC in the currency in which they are payable all sums which may be payable as if the Guarantor instead of the Borrower were the primary obligor, together with interest thereon at the rate per annum from time to time payable by the Borrower on such sums (and if no interest is payable or no rate applicable then at the Appropriate Rate charged by DFC at the relevant date under any Loan Agreement) from the time when such sums become payable by the Guarantor hereunder until payment of such sums in full (all such interest being hereinafter referred to as 'post demand interest')."

Clause 8.04 provides:-

"The Guarantor waives any right it may have of first requiring DFC to take any steps or proceedings against the Borrower or to enforce any guarantee or security of or from the Borrower or any other person and the Guarantor expressly agrees that DFC may enforce this guarantee against the Guarantor without first having recourse to any such guarantee or security and without taking any steps or proceedings against the Borrower or any other party."

The reasoning of the Court of Appeal, which persuaded them that a demand of Brookstock was a necessary condition of the respondents' liability as guarantors, is to be found in the following passage in the judgment of the Court:-

"It is submitted for the guarantors that a demand on Brookstock was a necessary condition to their liability. For DFC it is said that no notice of default or demand is required once an event listed in clause 5.03 has occurred and those referred to in paras. (a) and (j) had happened.

There is an apparent conflict between clause 1.02 which provides that the Borrower will pay DFC on demand and that demand may only be made if one or other of the events in clause 5.03 has happened and clause 5.01 which provides that all moneys become due without notice or demand on the happening of any of the events listed.

The debenture is a floating debenture made the primary object of clause 5.01 is, we think, to bring about the crystallisation of the charges. The provide that moneys become due and payable on the happening of the event which cystallises the charge is usual and, no doubt, prudent. In the present case, however, to give the clause full effect according to its tenor requires the word 'further' in the phrase 'further demand' to be read as 'other' and, much more importantly, renders otiose the provisions of clause 1.02(b) as to when demand may

be made. If on the other hand demand must be made before moneys secured become due clause 5.01 must be read down.

The point is not free from difficulty but we consider the proper conclusion is that a demand on Brookstock was necessary and as it was not made the moneys had not become due and the guarantors are not, as yet, liable. We reach that conclusion for three reasons. First, to read the debenture that way gives full effect to the earlier clause and at least partial effect to the later. If primacy is given to clause 5.01 the damage to the earlier clause is much greater. Secondly, the events which are set out in clause 5.03 which either trigger the right to demand or render the principal repayable include some which depend on the opinion of DFC. It is enough to refer to (j) set out above. Without notice from DFC the borrower could not know whether DFC had formed the opinion and hence could not know of its immediate liability. Thirdly, to read DFC's printed form in the way we prefer is to read it against DFC.

The conclusion we have reached is sufficient to dispose of the appeals and we do not find it necessary to examine the many other grounds advanced in their support."

Their Lordships have considered the terms of the debenture, with the assistance of counsel (to whom they are much indebted); and they have formed a different view of those terms from that which found favour with the Court of Appeal.

Their Lordships approach the matter as follows. They start with clause 5.01. In their Lordships' opinion, this clause means what it says, viz., that upon the occurrence of any one or more of the events listed in clause 5.03, (1) all moneys secured by the debenture shall become immediately due and payable without the necessity for any notice of default or further demand by DFC, and (2) the security shall attach and become fixed as regards all the assets, etc., charged by the debenture. They are unable to give to the words "further demand" the meaning attributed to them by the Court of Appeal. To do so, would be inconsistent with the provision in the clause that all moneys shall become immediately due and payable; it would also be inconsistent with the words "without the necessity of ...", since the function of this and the following words is to ensure that nothing shall detract from the moneys becoming immediately due and payable. It follows that, upon the happening of one or both of the events relied upon by DFC under clause 5.03(a) and (j), all moneys secured by the debenture did become immediately due and payable.

That having happened, DFC had to consider how to exercise their rights arising from the default. Clause 5.02 provides that they can in such event pursue any of the rights, powers and remedies conferred upon it by the debenture. Let it be supposed that DFC wished to have recourse against the Borrower, Brookstock. For that purpose, the relevant provision would be clause 1.02. That clause provides that the Borrower will pay to DFC on demand all amounts of Principal together with interest and other charges; but that DFC shall not have the right to make demand under the debenture for all such monies other than those due and payable in terms of the relevant Loan Agreement unless and until one of the events specified in (a) or (b) shall have occurred, (b) referring to the occurrence of any event of default listed in clause 5.03. It follows that, if DFC had wished to claim all such monies from Brookstock, it would have been necessary for it to make a demand upon Brookstock under clause 1.02 before commencing proceedings against it.

However, DFC did not wish to proceed against Brookstock (no doubt because of lack of assets), and instead decided to proceed against the three respondents as guarantors. For this purpose, the relevant provision is clause 8.01, which provides that if and each time the Borrower shall be in default in the payment of any sum whatsoever under any Loan Agreement, the guarantor will immediately pay to DFC all sums which may be payable as if the Guarantor instead of the Borrower was the primary obligor. Now, if the Guarantor instead of the Borrower were the primary obligor, it would follow that, by virtue of clause 1.02, a demand would have to be made upon the Guarantor instead of the Borrower. It was on that basis, no doubt, that such a notice was served by DFC upon the three respondents in the present case. Their Lordships cannot discern any requirement in clause 8.01 that a demand should in such circumstances be served upon the Borrower as well as upon the Guarantor; this is scarcely surprising, since such an additional notice would, in the circumstances, appear to serve no useful purpose. In any event, DFC could if necessary take advantage of the waiver by the Guarantor in the closing words of clause 8.04.

Before their Lordships, Mr. Roberts appeared in person. He advanced a further argument, as follows. The guarantee in clause 8.01(a) and (b) is in respect of the obligations of the Borrower under the Loan Agreement; and, consistently with that, the undertaking of the Guarantor contained in the paragraph following upon (b) is conditioned by the words "if and each time that the Borrower shall be in default in the payment of any sum whatsoever due under the Loan Agreement". But, submitted Mr. Roberts, DFC was claiming from the respondents the total amount of principal interest outstanding under the two agreements; such sums were

payable by the Borrower, not under the agreements, but under the debenture by virtue of clauses 5.01 and 5.02. It followed, he submitted, that clause 8.01 has no application in such a case. Their Lordships are, however, unable to accept this argument. The loans were advanced under the Loan Agreements, and so were in each case repayable under the relevant Loan Agreement. Under the terms of the Loan Agreements, the date for repayment was fixed as the maturity date. By virtue of clause 5.01 of the debenture, the date for repayment was varied, so that the loans became immediately repayable. That did not however alter the fact that it was under the Loan Agreements that the loans were repayable, and indeed any outstanding interest accrued due at the date of the relevant event of default was likewise payable under the relevant Loan Agreement. This analysis is reflected in clause 8.01(b) of the debenture, which refers to sums payable to DFC by the Borrower under any Loan Agreement when and as the same shall become due (whether at maturity, by acceleration or otherwise). It follows that the guarantee contained in clause 8.01 of the debenture applies in respect of such sums.

For these reasons, their Lordships will humbly advise Her Majesty that the appeal should be allowed, and that the matter should be remitted to the Court of Appeal to enable them to consider the other issues which were raised by the respondents on the appeal before them which they did not find it necessary to consider having regard to the view which they formed on the issue of the necessity of a demand upon Brookstock. Having regard to the nature of those issues, their Lordships are unwilling to consider them without the benefit of any view expressed by the Court of Appeal, especially in the context of an application for summary judgment under the procedure applicable in New Zealand. The first and third respondents must pay the costs of DFC before their Lordships. The costs of the first hearing before the Court of Appeal will be reserved to the Court of Appeal.