Privy Council Appeal No. 51 of 1989

Elders Pastoral Limited *Appellant*

v.

The Bank of New Zealand *Respondent*

FROM

THE COURT OF APPEAL OF NEW ZEALAND

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 22ND OCTOBER 1990

Present at the hearing:-

LORD BRIDGE OF HARWICH
LORD TEMPLEMAN
LORD GRIFFITHS
LORD ACKNER
LORD GOFF OF CHIEVELEY

*[Delivered by **Lord Templeman**]*

By a stock security dated 11th June 1987 and made between the respondent Bank of New Zealand ("the bank") of the one part and William Neville Gunn ("the grantor") of the other part, the grantor assigned and transferred to the bank the flocks of sheep and cattle and other stock enumerated in the first schedule, including the natural increase of stock depastured upon the farm of the grantor described in the second schedule. The assignment and transfer were declared to be by way of mortgage for securing the payment by the grantor to the bank upon demand of all moneys then or thereafter owing by the grantor to the bank. The Chattels Transfer Act 1924, as amended, ("the Act of 1924") provided for registration of the stock security being an instrument transferring the property in chattels by way of mortgage and the stock security was duly registered.

By section 50 of the Act of 1924 and clause 9 of the fourth schedule, there is implied in every instrument by way of security over stock a covenant by the grantor that he will not sell mortgaged stock except in the ordinary course of business. Section 54 provides that the implied covenants may be negatived, modified, or altered, or others may be added to them, by express words in the instrument. The provisions of clause 9 of the fourth schedule were added to by clause 15 of the stock security which, so far as relevant, provided that:-

"... (in the absence of any direction to the contrary by the Bank) all moneys payable in respect of the sale of any of the said stock ... shall be paid to the Bank whose receipt therefor shall be a sufficient discharge for or on account of the Grantor/s and the Grantor/s shall direct every purchaser ... accordingly."

By section 4(1) of the Act of 1924:-

"... all persons shall be deemed to have notice of an instrument and of the contents thereof when and so soon as such instrument has been registered as provided by this Act:"

On 13th January 1988 the appellants Elders Pastoral Limited ("Elders") as agents for the grantor sold some of the mortgaged stock and received the purchase price from the purchaser. The bank claim the net proceeds of sale from Elders and seek summary judgment on the grounds *inter alia* that clause 15 of the stock security created an equitable assignment to the bank by way of charge of the purchase price payable by the purchaser and that by virtue of section 4(1) of the Act of 1924 Elders had notice of that assignment. Elders deny that clause 15 created an equitable assignment and deny that section 4(1) gave notice to Elders of the provisions of clause 15 relating to the proceeds of sale of mortgaged stock. Elders claim to have appropriated the net proceeds of sale of the stock sold by Elders in satisfaction of an outstanding debt owed by the grantor to Elders.

The first question is whether clause 15 of the stock security created an equitable assignment by way of charge on a future chose in action, namely the right of the grantor to receive and recover from a purchaser the sale price of stock mortgaged to the bank. The requirements of an equitable assignment of a debt were reaffirmed in *William Brandt's Sons and Co. v. Dunlop Rubber Company Limited* [1905] A.C. 454. The document creating the assignment need not purport to be an assignment nor use the language of an assignment. Lord Macnaghten said, at page 462:-

"An equitable assignment does not always take that form. It may be addressed to the debtor. It may be couched in the language of command. It may be a courteous request. It may assume the form of mere permission. The language is immaterial if the meaning is plain. All that is necessary is that the debtor should be given to understand that the debt is being made over by the creditor to some third person. If the debtor ignores such a notice, he does so at his peril. If the assignment be for valuable consideration and communicated to the third person, it cannot be revoked by the creditor or safely disregarded by the debtor."

In the present case clause 15 gives to understand that the future proceeds of sale of mortgaged stock shall be made over by the grantor, to some third party, the bank. A promise by a debtor to a creditor that a sum owed or which will or may become due to the debtor from a third party shall be paid to the creditor by the third party is a clear form of equitable assignment, particularly when the promise is given for valuable consideration, in this case the grant of loan facilities to the grantor by the bank, and particularly where the debt assigned arises out of a disposition of property mortgaged to the creditor. Clause 15 contains an equitable assignment by way of charge of a future chose in action, namely the right of the grantor to receive from the purchaser the proceeds of sale of mortgaged stock sold to the purchaser. Clause 15 shows an intention that as the stock sold ceases to be charged to the bank, so the charge attaches to the proceeds of sale of that stock.

On behalf of Elders it was submitted that the fact that clause 15 permitted the bank to direct that the purchase price should not be paid to the bank and the fact that the grantor agreed to direct the purchaser to pay the bank in some way prevented the purchaser and Elders from understanding that the purchase price had been assigned to the bank and that they must comply with the provisions of clause 15 whether the grantor so directed or not. But these provisions only served to emphasise that the purchase price was charged to the bank (which might of course release the charge before or after the sale) and that the grantor had no right to receive the purchase price. The purchaser and Elders were not entitled to assume that the bank has issued a "direction to the contrary". The purchaser and Elders were entitled and bound to insist on paying the bank unless the grantor produced the requisite direction to the contrary from the bank.

It was not argued that the fact that the debt in respect of the purchase price was not in existence when the stock security was executed and could not come into existence until the mortgage stock was sold in some way prevented the debt being charged in equity in favour of the bank pursuant to clause 15. In *Tailby v. Official Receiver* [1888] 13 App. Cas 523 an assignment of future book debts was held to be effective and Lord Macnaghten said at page 543:-

> "It has long been settled that future property, possibilities and expectancies are assignable in equity for value. The mode or form of assignment is absolutely immaterial provided the intention of the parties is clear. To effectuate the intention an assignment for value, in terms present and immediate, has always been regarded in equity as a contract binding on the conscience of the assignor and so binding the subject matter of the contract when it comes into existence, if it is of such a

> nature and so described as to be capable of being ascertained and identified."

In the present case the assignment of the future right to the proceeds of sale of mortgaged stock was made for value, namely the making of advances by the bank to the grantor. The intention was clear that these proceeds of sale should be paid to the bank as mortgagee. The subject matter of the contract namely the proceeds of sale when the mortgaged stock was sold was ascertainable and identified.

The construction and effect of clause 15 of the stock security did not figure largely in the courts below. Cooke P. said that:-

> "I do not think that clause 15 goes so far as to amount to a contract by the farmer to assign a future chose in action; there is a contrast with certain express provisions of clause 19 about dairy factory moneys."

But clause 15 contains an express provision that the purchase price of mortgaged stock shall be paid to the bank and imposes a positive obligation on the grantor to direct the purchaser to pay the bank. Somers J. said:-

> "I am of opinion that the provisions of Clause 15 are not sufficiently clear to amount to a contract to assign future property. The clause contains a requirement that the purchase moneys be paid to the Bank and a promise by Mr. Gunn so to direct purchasers. Had an assignment been intended it is to be expected that his obligation would be to give notice of the Bank's right. The security is a running and continuing security, it is to apply whether or not Mr. Gunn is in credit with the Bank. The possibility of such a circumstance also suggests assignment was not intended. The distinction between a contractual obligation short of assignment and assignment itself is apparent from Clause 19 of the security with which the present clause may be compared."

The Board consider that the express provisions of clause 15 that the purchase moneys must be paid to the bank and that the grantor must give notice to the purchaser that the moneys must be paid to the bank, sufficiently clearly assigned to the bank the right to receive the purchase money as mortgagee and in the place of the mortgaged stock sold to the purchaser. The grantor, Mr. Gunn was placed under an obligation to give notice of the bank's right to receive the purchase moneys. The fact that the security was running and continuing and the possibility that Mr. Gunn might be in credit with the bank cannot affect the construction of clause 15. The grantor could always draw cheques on the bank to the extent of his credit balance and up to the agreed limit of any

overdraft facility. The clause 15 assignment of the proceeds of sale of mortgaged stock to the bank however protected the bank by putting them in control of the proceeds of sale so that they could insist that any obligation of the grantor to the bank be reduced by the amount of the proceeds of sale.

Clause 19 of the stock security upon which Cooke P. and Somers J. relied consists of a covenant by the grantor to:-

> "Deliver all milk, cream, butter fat, cheese and other milk products the produce of the cows for the time being from time to time subject to this security ... to such company, firm or person as the bank shall appoint and will assign to the bank the moneys payable by such company, firm or person therefor and will from time to time if and when the bank shall so stipulate sign and deliver to the bank such deed or deeds of assignment or irrevocable order or orders to ensure the payment to the bank of the said moneys or such part thereof as the bank shall require."

Milk products were not mortgaged chattels and no reasonable purchaser of milk products from a farmer would search under the Act of 1924 or pay the bank instead of the farmer unless the bank produced a written assignment or order of the farmer. Hence the provisions of clause 19 which are presumably only enforced by the bank when the financial position of the farmer causes the bank to interfere with the day to day running and financing of the farm. Clause 15 on the other hand dealt with mortgaged chattels and applied to every purchaser of every sale of mortgaged chattels comprised in the registered security. The obligation of such a purchaser to pay the bank is clearly set forth in clause 15 and needs no supplementary assignment or order. Their Lordships do not consider that clause 19 affects the construction of clause 15 whereby the proceeds of sale of mortgage stock are mortgaged to the bank.

When the grantor agreed that all monies payable in respect of the sale of mortgaged stock should be paid to the bank he thereby conferred on the bank the right to receive those moneys. The simplest form of an equitable assignment of a debt is an agreement by a debtor with a creditor that a debt due or to become due to the debtor from a third party shall be paid by the third party to the creditor. Of course the third party is only bound by that assignment if he receives notice of the agreement by registration or actual notice. The obligation imposed by the stock security on the grantor to direct the purchaser to pay the bank ensured, so far as possible, that the purchaser would receive actual notice of the rights of the bank as well as the statutory implied notice arising from registration of the security under the Act of 1924. Accordingly

their Lordships take the view that clause 15 effected an equitable assignment of the proceeds of sale of the mortgaged stock.

The second question is whether the purchaser and Elders had notice of the equitable assignment created by clause 15 of the stock security.

Section 4 of the Act of 1924 provides that:-

> "(1) ... all persons shall be deemed to have notice of an instrument and of the contents thereof when and so soon as such instrument has been registered as provided by this Act:"

A registrable instrument, defined by section 2 of the Act includes:-

> "Any ... mortgage or any other document that transfers ... the property in ... chattels."

Chattels, as defined by section 2 include:-

> "Stock and the natural increase of stock."

Stock is defined to include any sheep, cattle and horses and embraces the stock mortgaged by the stock security.

Thus the stock security was a registrable instrument and clause 4(1) gave notice to the world of its contents. On behalf of Elders it was submitted that the legislature cannot have intended that the registration should give notice of every provision contained in a registrable instrument whether or not that provision relates to chattels. Proceeds of sale of chattels are not themselves chattels and so, it was argued, registration under the Act does not give notice of any provision dealing with proceeds of sale. Reliance was placed on section 4(2) which provides that:-

> "... all persons shall be deemed to have notice of a security granted wholly or partly upon chattels by a company registered under the Companies Act ... and of the contents of such security, so far as it relates to chattels, immediately upon the registration of such security in the manner provided by the Companies Act."

A registered instrument which contained a positive prohibition against a sale of mortgaged chattels by the grantor or provided that such a sale required the prior consent of the mortgagee would plainly relate to chattels and would be binding on purchasers and auctioneers. It would be strange if a registered instrument gave notice of a prohibition against a sale of mortgaged chattels but did not give notice of a provision which required the purchase price of mortgaged chattels to be paid to the mortgagee. Clause 15 relates to chattels and deals with the sale of

chattels. Clause 15 gave notice that the stock security had not modified the provisions of the Act of 1924 which enabled the purchaser to purchase mortgaged chattels free from the mortgage and at the same time gave a purchaser notice that on any such purchase he must pay the purchase price to the mortgagee.

Counsel for Elders relied on the decision of the Court of Appeal in *Dempsey and The National Bank of New Zealand Limited v. The Traders Finance Corporation Limited* [1933] NZLR 1258. In that case a company registered under the Companies Act a debenture which created a floating charge, prohibited the company from creating any mortgage or charge in priority to the debenture and prohibited the sale and disposal of any property except merchandise and that only in the ordinary course of business. The company later mortgaged its interests under hire purchase agreements relating to motor vehicles. The majority of the Court of Appeal held that registration of a floating charge was only notice of the existence of the charge and not of its contents because, per Smith J. at page 1290:-

> "A floating charge belongs to a class of documents which may or may not, but does not necessarily, affect the title to property and the court will not, in respect of such document which affect commercial transactions, apply the doctrine of constructive notice though it is sought to found it on the public registration of such documents."

In the present case the fixed charge on the stock comprised in the stock security and on the proceeds of sale of such mortgaged stock affects the title to the mortgaged stock and the title to the proceeds of sale. The majority also held that the hire purchase agreements constituted a mode of disposal permitted by the debenture and that the mortgagee of the benefit of the hire purchase agreements had no notice under section 4(2) of the Act of 1924 or otherwise that the acquisition of such rights which were choses in action and not chattels constituted an infringement of the restrictive qualifications of the debenture. In the present case the mode of disposal of the mortgaged stock permitted by the Act of 1924 and the stock security imposes on the purchaser an obligation to pay the proceeds of disposal to the bank. The purchaser has notice that his right to acquire the mortgaged chattels involved him in an obligation to pay the purchase price to the bank.

In the opinion of the Board, the contents of the stock security of which all persons are deemed to have notice include those contents which are relevant to any dealing with chattels comprised in the instrument. The purchaser who asserts that, under and by virtue of the Act of 1924 and the stock security, the grantor was entitled to sell and the purchaser was entitled to purchase mortgage chattels freed and discharged from

the mortgage without the concurrence of the mortgagee cannot at the same time deny that he had notice under and by virtue of section 4(1) of the Act of 1924 of the contents of the stock security which require him to pay the purchase price to the mortgagee. The auctioneer who sells the mortgaged chattels and receives the purchase price is in no different position.

It was submitted that the result would produce some inconvenience. If there is any inconvenience it is due to the legislature, for good reason, enacting that registration of a stock security shall be notice of the contents of the instrument and due to the stock security which, for good reason, assigned to the bank the proceeds of sale of mortgaged chattels. It is not clear that great inconvenience will be caused. A purchaser of chattels may either trust his vendor or trust the auctioneer or carry out a search against the vendor. An auctioneer may either know or enquire from the vendor or search against the vendor to ascertain if there is any stock security which either forbids a sale without the prior consent of the mortgagee or requires the proceeds of sale to be paid to the mortgagee. It is likely that an auctioneer will be aware of the terms of the standard form of the stock security issued by the bank. It is likely that any prudent lender on the security of stock will also require the proceeds of sale of mortgaged stock to be paid to the lender. The purchaser need not pay and the auctioneer need not transmit the purchase moneys to the vendor until it is clear that no registered instrument requires payment to some other person. The protection afforded by a registered instrument under the Act of 1924 would be much weakened if a mortgagee of mortgaged chattels was unable to secure the proceeds of sale of the mortgaged chattels.

Their Lordships conclude that the proceeds of sale of stock comprised in the stock security were charged to the bank and that Elders had notice of that charge as a result of the registration of that stock security under the Act of 1924.

The Court of Appeal considered that the stock security drafted by the bank did not charge the proceeds of sale of the mortgaged stock. The court decided that even if there was no charge, Elders held the proceeds of sale as constructive trustees for the bank. Having decided that clause 15 of the stock security did create a charge, their Lordships do not find it necessary to consider whether the judgment of the Court of Appeal should be affirmed on other grounds. Their Lordships will humbly advise Her Majesty that this appeal should be dismissed. Elders must pay the costs of the bank before the Board.