Privy Council Appeal No. 27 of 1973

Peter Thomas Fahey – – – – – *Appellant*

v.

M.S.D. Speirs Limited – – – – – *Respondents*

FROM

THE COURT OF APPEAL OF NEW ZEALAND

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 24TH OCTOBER 1974

Present at the Hearing:

LORD MORRIS OF BORTH-Y-GEST
LORD WILBERFORCE
LORD HAILSHAM OF SAINT MARYLEBONE
LORD CROSS OF CHELSEA
LORD SALMON

[*Delivered by* LORD MORRIS OF BORTH-Y-GEST]

In respect of a guarantee which he signed on the 2nd December 1968 the appellant (Mr. P. T. Fahey) was held, in an action tried by Quilliam J., to be liable to pay the sum of $11,853·43 to the respondents (M. S. D. Speirs Limited). He appealed to the Court of Appeal (McCarthy P., Richmond and Beattie JJ.). The appeal was dismissed. Leave to appeal to Her Majesty in Council was given.

In the course of his business as a building contractor the appellant needed to purchase building materials. The respondents are suppliers of such. In 1963 and in certain subsequent years the appellant purchased supplies from the respondents.

In April 1967 the respondents found it necessary to send a circular letter to all their customers including the appellant. After referring to trade comments which were to the effect that any over-extension of credit resulted in detriment to the building industry the respondents called the attention of their customers to the company's credit policy. It applied alike to trade and retail accounts. The letter (dated the 5th April)

set out that payment for materials was due on the 20th of the month following supply, that a discount of 2½% would be allowed provided the account was paid on its due date; that if an account became 3 months overdue further credit would be withheld and that there would be an interest charge of 1% per month until payment: and that legal action for the recovery of the full amount due might be instituted once an account became 3 months overdue. The policy was to be rigidly enforced.

In the following November (*i.e.* November 1967) the appellant passed over his business to a Limited Company which was formed. It was called—Fahey Construction Company Limited. The evidence called by the respondents did not deal with the shareholding in the company. The appellant did not give evidence and called no evidence. It was acknowledged however that he was the head of and that he managed the business of the company. After it was formed purchases of building materials from the respondents continued to be made though they were purchases by the newly formed company. In respect of purchases made before the company was formed the appellant continued for a time to owe money personally to the respondents but by March 1968 his personal account was cleared.

The new company soon became in arrears with its account to the respondents. By the 1st August 1968 a sum of $6,859·84 was owing: more than half of that amount was more than 3 months overdue. The respondents communicated (on the 20th August 1968) with the appellant about "the unsatisfactory state of your account". The reference to "your" account was a reference to his company's account. A meeting took place on the 30th August 1968 at which the appellant was told that the company's account must be brought up to date and that, if it were not, security would be required in the form of a mortgage or of a personal guarantee by him.

It is common ground and indeed at the trial it was expressly admitted that at various meetings which took place the appellant, though demurring to the payment of interest on undue amounts, agreed that his company would have to pay such interest.

The evidence established and it was held both by the learned Judge at the trial and by the Court of Appeal that the practice followed by the respondents upon receiving a payment from a customer was to apply the payment first towards outstanding interest, next towards the reduction of those accounts which were three months or more overdue and finally in reduction of the balance of the account. That practice was followed in relation to the respondents' account in the period before Fahey Construction Co. Ltd. was formed and after November 1967 in relation to the account of that company.

So matters continued. In spite of what had been said to the respondents in August 1968 the indebtedness of the Fahey company continued to increase. By the 1st December 1968 it had reached the amount of $10,070·06. The appellant was seen again and was told by a representative of the respondents that the account must be brought up to date and that if it were not the mortgage or guarantee previously referred to would be required: he was told that unless one of these courses was followed there could not be a continuation of supplies. A suggestion that the appellant should sign a guarantee in the respondents' standard form was not acceptable to him. He said however that he knew what was required and that he would write out his own form of guarantee. The result was

that at a later date (*i.e.* on the 2nd December 1968) he produced and handed over his guarantee. It was in the following terms:—

> M. S. D. Speirs Ltd.
> Elizabeth Street
> Waikanae
>
> I Peter T. Fahey hereby guarantee to pay for any materials which are purchased from M. S. D. Speirs Ltd. by Fahey Construction Co. Ltd. in the event of Fahey Construction Co. Ltd. not being in a position to do so.
>
> (signed)
> Peter T. Fahey

Thereafter the Fahey company continued to order and to receive supplies from the respondents. Any payments that were thereafter made were appropriated by the respondents in exactly the same manner as before. Certain payments made by the Fahey company may be noted. At the time of the giving of the guarantee the amount owing by them was $10,070·06. By the end of December 1968 a payment of $3,000 had been made though new purchases made during December involved amounts less than a quarter of that amount. Three other payments (respectively of $2,000, $5,000 and $3,500) were made before the end of July 1969. They seem clearly to have been payments generally on account of the indebtedness of the Fahey company. In total ($13,500) the four payments were more than enough to pay the amount due and outstanding on the 1st December 1968 (*i.e.* $10,070·06).

The amount of the indebtedness of the company fluctuated and though certain payments were made the indebtedness (including interest) reached the sum of $15,916·10 by the end of May 1971. The supply of materials then apparently ceased. Demands for payment of the amount owing were made both upon the Fahey company and upon the appellant under his guarantee. A writ against him was issued on the 7th July 1971. The amount of $15,916·10 was claimed. Later the Fahey company went into liquidation. A first dividend of $4,062·47 was paid in the liquidation. The amount thereafter remaining unpaid was $11,853·43. For that amount the appellant has been held liable.

Both before the learned Judge and before the Court of Appeal it was unsuccessfully contended on behalf of the appellant that the document of the 2nd December 1968 was an indemnity and not a guarantee. That contention was not renewed when this appeal was argued before their Lordships. It being accepted (and as their Lordships think rightly accepted) that the document was a guarantee, various arguments as to its construction were presented.

One of these was that the guarantee did not extend to cover any such part of the amount claimed as consisted of an interest element. In their Lordships' view such a construction would put a meaning on the words of the guarantee which would be wholly divorced from business reality. What both parties undoubtedly had in mind was that the appellant was promising that in the event of the inability and failure of the Fahey company to pay, he (the appellant) would pay the amount which the Fahey company should have paid and had to pay for the materials which they purchased. The appellant knew fully and precisely the terms upon which the respondents would supply materials. The appellant himself, as was accepted, had agreed that " his " company would have

to pay interest according to the arrangement made. What the Fahey company had " to pay for any materials " was the amount laid down according to the terms upon which purchases could be made. All the surrounding circumstances show that when the guarantee was signed both parties knew and had in mind the terms upon which supplies had been and were being purchased and the terms upon which future purchases of supplies would be made. They knew therefore what were the amounts that the Fahey company would have to pay for any materials which they purchased. Their Lordships are in agreement both with the learned Judge and with the Court of Appeal in rejecting the contention.

The next contention as to the construction of the guarantee related to the words " any materials which are purchased ". As has been pointed out the amount owing by the Fahey company in respect of their purchases made before the date of the guarantee (2nd December 1968) was $10,070·06. Did the guarantee apply to that indebtedness and to all future indebtednesses for materials purchased or did it apply only to the indebtednesses which were incurred after the date of the guarantee? On this question the conclusion of the learned Judge that the guarantee covered the company's indebtedness prior to the date of the guarantee was not shared by the Court of Appeal. Their Lordships think that this matter must be resolved by construing the guarantee. There is much to be said for the view that on the facts as found by the learned Judge it would have been reasonable for the respondents to require or to insist on having a guarantee which covered existing as well as future indebtedness and that it would have been only reasonable for the appellant to have given such a guarantee and so to avoid the risk that no further materials would be supplied until the account was cleared. Regard must be had however not to what might have been done or to what would have been reasonable but to what was actually done. Though the guarantee was not drawn professionally and appears to have been in a form drafted and written out by the appellant himself the respondents accepted it and cannot now alter it or improve its language. Giving to the language a fair and reasonable interpretation their Lordships consider, in agreement with the Court of Appeal, that the guarantee related to future purchases of materials (*i.e.* to those made after the date of the guarantee).

The next contention raised a point of no little importance in regard to appropriation. What the respondents in fact did after the 2nd December 1968 was to appropriate any payments received by them from the Fahey company just in the same manner as they had throughout adopted. The question is raised whether there was any reason why they should not do so. When making payments the Fahey company did not seek to allocate or appropriate their payments to any particular item or items of indebtedness. There was no agreement made between the appellant and the respondents that payments made by the Fahey company were to be appropriated in any particular way. There is no suggestion that the appellant ever invited such an agreement.

So the question is now raised whether in those circumstances the appellant can say that as the terms of the guarantee related to what may be called future indebtedness any future receipts ought first to be allocated, so far as concerns the liability of the guarantor, in satisfaction of new indebtedness arising after the date of the guarantee.

If a line were drawn as at the 2nd December 1968 leaving the sum of $10,070·06 as an item of old indebtedness above that line and if any

future receipts had to be allocated or appropriated in satisfaction of new indebtedness below the line (only allowing the amount of any receipts over and above the amount of new indebtedness to be used to diminish the amount of the above-the-line old indebtedness) then it is said that an account taken on such basis would show a figure very considerably lower than the amount claimed in these proceedings by the respondents: there would be some variation according as to whether new indebtedness figures included or did not include any interest element but on either basis there would result a figure considerably lower than that claimed.

In the dealings between the respondents and the Fahey company there was no difference between the accounting methods in the period after the 2nd December 1968 as compared with those in the period before such date. No line was drawn as at that date. Furthermore it seems clear that the appellant who was managing the Fahey company and who knew and operated its affairs never contemplated that there would be any change after the 2nd December 1968 and never suggested or thought that some new and separate account would as from that date be opened.

Was there any reason therefore in this case why the respondents should not, so far as concerned the appellant's liability as guarantor, do as they had always done and appropriate payments received from the Fahey company against earliest indebtedness in pursuance of their practice?

There having been no express agreement made in regard to appropriation when the guarantee was given the contention that is made on behalf of the appellant is that it was an implied term of the guarantee agreement that the appellant as guarantor would be entitled, in relief of his obligations under the guarantee, to the benefit of future payments thereafter to be made by the debtor (the Fahey company) and that he was so entitled no matter how future payments were appropriated as between the respondents and the Fahey company. The question so raised must be decided after a consideration both of general legal principles and of the particular facts and circumstances of the present case.

The general principle in regard to appropriation is thus stated in *Rowlatt on Principal and Surety* (3rd Edition p. 124):—

> "The question whether payments made by the principal debtor, not being dividends in his bankruptcy, are to be appropriated in discharge or reduction of the guaranteed or some other indebtedness, is one which, in the absence of special agreement between the creditor and the surety, must be determined as if it arose merely between the creditor and the principal debtor, a surety having no right of his own to dictate either to the creditor or the debtor how payments made by the latter are to be appropriated".

To a similar effect in *Halsbury's Laws of England* (3rd edition Vol. 18) it is said (at p. 493):—

> "The mere existence of a suretyship does not, in the absence of express contract, take away from the principal debtor and creditor those powers which they would otherwise possess of appropriating payment".

Support for the proposition so stated is found in the judgment of Lord Selborne L.C. in—*In re Sherry—London and County Banking Co. v. Terry* (1884) 25 Ch. D 692.

The terms of particular contracts of guarantee may be infinitely varied and decisions which turn upon the construction of particular written contracts (*e.g. Kinnaird v. Webster* (1878) 10 Ch. D. 139) do not call for consideration. In the interesting case of *Bank of Australasia v. Wilson* (1885) 3 N.Z.L.R.C.A.130 questions arose (i) as to the meaning and implications of words in a guarantee to a Bank " in respect of transactions with the Bank after the 12th February 1883 " (one question being whether the intention of the parties was that a fresh account was to be opened without any balance from the old account being brought down) and (ii) as to whether the guarantor was released from his guarantee by reason of the non-disclosure to him of an agreement (the existence of which he could not have expected) between the debtor and the Bank to the effect that sums of money would be drawn by the debtor out of the new guaranteed account and be applied in payment of old debts to the Bank.

In the present case there are none of the complications that arose in that case. In the present case there was no room for any misunderstanding. The appellant knew all the facts and circumstances. He neither sought nor suggested that there should be any special agreement in regard to appropriation. There was no break or line drawn in the arrangements or transactions between the respondents and the Fahey company: no new or separate account was opened.

On behalf of the appellant it is not suggested that the mere giving of a guarantee has the result that a creditor's rights as to appropriation are affected. The general principle of law above noted is not contested. The only point that is taken is that it should be held that there was an implied term that the guarantor would be entitled in relief of his obligations under the guarantee to the benefit of any payments thereafter to be made by the debtor. It is contended that this implication is necessary in order to give business efficacy to the agreement. Their Lordships can see no ground for this contention. Without the suggested implied term the contract has full efficacy. Every indication from the facts of the case is that it never occurred to the appellant that there should be any special agreement in regard to appropriation: every indication furthermore is that the respondents would not have entertained any proposal to that effect.

Lastly it was contended that by reason of the fact that the respondents' terms of business included the provisions as to interest the company was a money lender within the meaning of the Moneylenders Act 1908 and was not registered. Section 2 of that Act shows that with certain exceptions the term moneylender includes every person (whether an individual, a firm, a society or a corporate body) whose business is that of moneylending or who advertises or announces himself or holds himself out in any way as carrying on that business. Their Lordships see no evidence at all that the respondents were carrying on the " business " of moneylending. Their letter to their customers in April 1967 showed that their genuine concern and desire was that accounts should be paid and should not be outstanding. The reason why interest was to be charged on overdue amounts was so that prompt payment would be encouraged. There were none of the elements of a disguised loan transaction. The transactions were genuine sale transactions. To regard

purchasers who were dilatory in their payments to a vendor as being borrowers from a moneylender would be wholly irrational.

In agreement with the judgment of the Court of Appeal their Lordships consider that the contentions submitted on behalf of the appellant must fail. Their Lordships will therefore humbly advise Her Majesty that the appeal should be dismissed. The appellant must pay the respondents' costs.

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In the Privy Council

PETER THOMAS FAHEY

v.

M.S.D. SPEIRS LIMITED

DELIVERED BY
LORD MORRIS OF BORTH-Y-GEST

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