Privy Council Appeal No. 30 of 1994

Motor Vehicle Dealers Institute Incorporated *Appellants*

v.

UDC Finance (1991) Limited *Respondents*

FROM

THE COURT OF APPEAL OF NEW ZEALAND

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 15TH NOVEMBER 1994

Present at the hearing:-

LORD KEITH OF KINKEL
LORD MUSTILL
LORD WOOLF
LORD LLOYD OF BERWICK
LORD NICHOLLS OF BIRKENHEAD

*[Delivered by **Lord Lloyd of Berwick**]*

This is an appeal by leave of the Court of Appeal of New Zealand granted on 2nd May 1994. It concerns a claim by a finance company, UDC Finance (1991) Limited ("UDC") to obtain reimbursement from the Motor Vehicle Dealers Fidelity Guarantee Fund under section 35 of the Motor Vehicle Securities Act 1989. Master J.C.A. Thomson decided in favour of UDC at first instance, and his judgment was affirmed by the Court of Appeal. The Motor Vehicle Dealers Institute Incorporated now appeals to Her Majesty in Council. The respondents were not represented at the hearing of the appeal. Their Lordships were informed that the respondents were content to leave the matter in their Lordships' hands.

Section 35 of the 1989 Act has now been amended by section 4 of the Motor Vehicle Securities Amendment Act 1994. The effect of the amendment is to reverse the decision of the Court of Appeal. But the amending Act was not retrospective. As a result more than $1 million is said to depend on the outcome of this appeal.

Save in one respect, which their Lordships will mention in due course, the facts are not in dispute. On 27th November 1990 City Motor Services Limited ("City Motors")

entered into a stock financing contract called a Bailment Display Plan Agreement, with National Mutual Finance Limited, as UDC was then known. The purpose of the agreement was to provide for the purchase of motor vehicles by UDC at the request of City Motors, and the bailment back by UDC to City Motors of the vehicles so purchased. Title was to pass to UDC, but possession was to remain with City Motors. It was a term of the agreement that City Motors was to keep the vehicles in its possession at its premises, and was not to attempt to sell or dispose of the vehicles without UDC's prior consent in writing. In practice this term was disregarded. Between 15th January 1992 and 12th February 1992 a total of seven cars were sold by City Motors to members of the public in breach of the terms of the Bailment Agreement. City Motors failed to account for the sale proceeds, and on 13th February 1992 went into receivership. On 3rd November UDC made a claim for payment against City Motors under section 34 of the Act. City Motors failed to pay. So on 26th November 1992 UDC made a claim for reimbursement from the Fund under section 35.

It is convenient at this stage to set out the relevant provisions of the 1989 Act.

"24. Extinguishment of security interest in case of consumer purchase from dealer -

Where a consumer purchases a motor vehicle that is subject to a security interest from a dealer, -

(a) The security interest in that motor vehicle shall be extinguished; and

(b) The consumer shall acquire the vehicle free from the security interest; and

(c) Where title to the vehicle was vested in the holder of that security interest, title shall pass to the consumer.

...

26. Relevance of notice of security interest -

Sections 24 and 25 of this Act shall apply whether or not the dealer or the consumer has notice of the security interest, and whether or not the dealer is the debtor, except where -

(a) The security interest is disclosed to the consumer in writing before the contract of sale becomes binding on the consumer, or, as the case may be, before the hire purchase agreement or lease is entered into; or

(b) The security interest is created by or with the express consent of the consumer."

"Debtor" is defined by section 2 of the Act as the person who created the security interest.

"29. Rules for determining whether person has notice of security interest -

(1) For the purposes of this Act, a person has notice of a security interest if -

(a) The security interest is registered; or

(b) The person has actual knowledge of that security interest ...

34. Reimbursement of secured party by dealer with notice of security interest -

Where -

(a) A motor vehicle is purchased from a dealer; and

(b) The motor vehicle is subject to a security interest immediately before the time of purchase; and

(c) The dealer has notice of that security interest at the time when the purchase price is paid or the exchange is made; and

(d) The security interest in that motor vehicle is extinguished by virtue of section 24 or section 27 of this Act, -

the dealer shall pay to the secured party, within 7 working days of the date on which the secured party serves a claim for payment on the dealer, the amount outstanding in respect of the debt or other obligation secured by the security interest.

35. Reimbursement of secured party by Motor Vehicle Dealers Fidelity Guarantee Fund -

(1) Where -

(a) Any person purchases from a dealer a motor vehicle that is a motor vehicle within the meaning of section 2 of the Motor Vehicle Dealers Act 1975; and

(b) The dealer fails to comply with section 34 of this Act, -

the secured party may make a claim under Part III of the Motor Vehicle Dealers Act 1975 for payment by the Motor Vehicle Dealers Fidelity Guarantee Fund of the amount that the dealer is required by that section to pay to the secured party.

...

37. Subrogation of rights of action against debtor and dealer -

(1) Where payment is made to the secured party by the dealer pursuant to section 34 of this Act, or by the Motor Vehicle Dealers Fidelity Guarantee Fund pursuant to section 35 of this Act, the dealer or the Fund, as the case may be, shall be subrogated, to the extent of that payment, to all rights and remedies that, but for the subrogation, the secured party would have had against the debtor ...

62. Savings -

Except to the extent that this Act expressly provides otherwise, nothing in this Act shall -

(a) Prevent any purchaser of a motor vehicle acquiring title to the vehicle by virtue of any provision of the Sale of Goods Act 1908 or by virtue of any other enactment or rule of law; or

(b) Modify, restrict, or exclude any other right or remedy that a person would have had if this Act had not been enacted."

Section 35(1)(b) of the Act makes clear that the secured party can only claim against the Fund if the dealer has failed to comply with its obligation under section 34. This obligation depends on the fulfilment of four conditions set out in paragraphs (a) to (d). Mr. Reed, who appeared on behalf of the appellants, conceded that section 34(a) and (b) had been satisfied. The motor vehicles in question were purchased from a dealer, City Motors, and were subject to the security interest vested in UDC immediately before the time of purchase. But he submits that the conditions set out in section 34(c) and (d) were not satisfied. Their Lordships take these provisions in turn.

Did City Motors have notice of UDC's security interest at the time when the purchase price was paid by its customers? Clearly, City Motors had actual knowledge of the security interest, so the case fell within the literal terms of section 29 of the Act. But their Lordships are persuaded that this is not the meaning or effect of section 34(c). It would be an odd use of language to describe a dealer as having notice of a security interest when he is himself a party to the agreement creating that interest. The provision must therefore be directed to a security interest created by a third party, not the dealer from whom the secured party is claiming reimbursement under section 34. This is borne out both by the context and by other provisions of the Act.

As for the context, section 34 provides that where the conditions set out in (a) to (d) are met, the dealer shall pay the amount outstanding in respect of the debt within 7 working days. This provision cannot have been intended to apply to a dealer who is already contractually liable to

pay the whole debt. It would make no sense to require the dealer to pay within 7 working days when, as here, he is liable by contract to pay within 48 hours. The necessary inference is that section 34 does not apply when the dealer is himself the debtor under the contract creating the security interest.

As for other related provisions of the Act, section 26 provides that section 24 shall apply "whether or not the dealer ... has notice of the security interest, and whether or not the dealer is the debtor". If a dealer who has notice of a security interest includes a dealer who is himself the debtor, then the words "whether or not the dealer is the debtor" would be otiose. But section 26 draws a careful distinction between the two cases. Section 24 applies when the dealer is the debtor as well as when he has notice of the security interest. The former words are absent from section 34. The implication is clear that section 34 applies in the latter case, but not in the former.

Even clearer is the implication from section 37. It provides, *inter alia*, that where the dealer has paid the secured party, he shall be subrogated to all rights which the secured party would have had against the debtor. This makes sense where the debtor is a third party. It makes no sense at all where the dealer and the debtor are the same person.

Mr. Reed informed the Board that an argument based on section 34(c) was advanced both before the Master and the Court of Appeal. But it is not reflected anywhere in their judgments, perhaps because it was not put in the forefront of the case. Be that as it may, their Lordships are satisfied that it provides a complete answer to the claim put forward by UDC. City Motors was itself the debtor under the contract creating the security interest. The condition set out in section 34(c) was not, and could not be, fulfilled. It follows that City Motors was under no obligation created by section 34, and therefore that UDC had no right to claim reimbursement from the Fund under section 35.

Their Lordships turn to section 34(d). For section 34 to apply, the security interest must have been "extinguished by virtue of section 24". What is the meaning of these words? In particular, is the condition fulfilled where the title to the motor vehicles would have passed to the customers irrespective of section 24, by virtue of section 3 of the Mercantile Law Act 1908 or sections 23 or 27(1) of the Sale of Goods Act 1908? It is unnecessary to set out these provisions since it was conceded in the courts below that one or all of these exceptions to the rule "nemo dat quod non habet" would have applied on the facts of the present case. Accordingly title would have passed to the customers even if section 24 had never been enacted. The question

thus turns on whether, in these circumstances, the security interest could be said to have been extinguished by virtue of section 24.

It was pointed out by UDC in the court below that section 34(d) does not say "extinguished only by virtue of section 24". If therefore the security interest was extinguished by section 24, as well as by section 3 of the Mercantile Law Act or sections 23 or 27(1) of the Sale of Goods Act, then section 34(d) was satisfied. It was argued on behalf of the Fund that a security interest could not be said to have been extinguished by section 24 when it was "stifled before birth" by the Mercantile Law Act and the Sale of Goods Act: see *Dexter Motors Limited v. Mitcalfe* [1938] N.Z.L.R. 804 per Johnston J. at page 822.

The courts below accepted UDC's argument. Master Thomson's reasoning, approved by the Court of Appeal, was in brief that the Mercantile Law Act and the Sale of Goods Act were both made subject to the 1989 Act, and the former Act in particular did not apply (despite the concession) since UDC did not register its security interest as provided by section 3(1A) of that Act until after City Motors had gone into receivership. Their Lordships cannot accept this reasoning. It gives no effect to section 62 of the 1989 Act which specifically preserves the purchaser's remedies where he has acquired title by virtue of the Sale of Goods Act or any other enactment. The purpose of the amendments set out in the second schedule to the 1989 Act was not to abrogate the purchaser's remedies under those Acts, but to ensure that they tied in with the new remedies provided under the 1989 Act.

Their Lordships return to the critical expression "extinguished by virtue of section 24". It seems to their Lordships that these words are at the very least ambiguous. If so, then, as the Court of Appeal accepted, substantial weight must be given to more general considerations.

Prior to the 1989 Act, a purchaser in good faith could acquire a motor vehicle free of any security interest by virtue of section 18A(2) of the Chattels Transfer Act 1924. But that subsection applied only where the security interest was created by the dealer. One of the purposes of the 1989 Act, and the reason for the consequential exclusion of motor vehicles from the Chattels Transfer Act 1924, was to extend the protection afforded to the purchaser of a motor vehicle. This was achieved by section 24 of the Act. It enables the purchaser to override security interests even when they have been created by someone other than the dealer, as may happen when a motor vehicle has been subject to a customary hire purchase agreement, and in other cases.

But as a quid pro quo, the finance house was to be entitled to claim against the dealer, and ultimately against the Fund, if it registered its security interest under the 1989 Act, or if the dealer had actual knowledge of the security interest: see sections 29 and 34(c). In other words

the scheme of the Act was to compensate the finance house for loss of any right of repossession which it would have had before section 24 came into force. This limited purpose makes good commercial and legislative sense.

The alternative view is that the Act was intended to bring about a far-reaching change in the commercial relationship between dealers and finance houses, a change which would amount, in effect, to insuring the finance house against the dealer's insolvency at the Fund's expense. Faced with these alternatives, their Lordships prefer a construction which gives effect to the more limited legislative intent.

Thus in their Lordships' view the security interest in a motor vehicle is only extinguished within the meaning of section 34(d), if the secured party would have been entitled to repossess the vehicle but for the operation of section 24. In the present case it was conceded in the courts below that UDC would not have been entitled to repossess the vehicles. It follows that the condition set out in section 34(d) was not fulfilled and that Mr. Reed's argument succeeds under section 34(d) as well as section 34(c).

For the above reasons their Lordships will humbly advise Her Majesty that the appeal should be allowed. It is unnecessary to deal with an alternative argument, which was said to raise a disputed question of fact, that title to two of the vehicles never passed to UDC in the first place.

In conclusion their Lordships would like to express their indebtedness to an article by Professor McLauchlan in the February 1994 issue of the New Zealand Law Journal at page 59.

The respondents must pay to the appellants their costs before the Board and in the courts below.