**IN THE HIGH COURT OF NEW ZEALAND**
**NELSON REGISTRY**

**I TE KŌTI MATUA O AOTEAROA**
**WHAKATŪ ROHE**

**CIV-2020-442-62**
**[2024] NZHC 1225**

| | |
|---|---|
| UNDER | the Companies Act 1993 |
| IN THE MATTER OF | breaches of director's duties and breaches of contract |
| BETWEEN | FIRST NZ PROPERTIES LIMITED<br>Plaintiff |
| AND | MICHAEL JOHN MILLAR<br>First Defendant |
| | INVESTMENT SERVICES LIMITED<br>Second Defendant |
| | PAUL JOHN MEPHAN<br>Third Defendant |
| | CONTINUED… |

Hearing: 1–5, 8–9 and 12 May 2023

Counsel: B M Nathan, N Laing and E V Kittelty for the Plaintiffs
M J Radich and S A Wadworth for the First and Second Defendants
R J B Fowler KC for the Third Defendant in CIV-2020-442-62/63

Judgment: 16 May 2024

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**JUDGMENT OF GWYN J**

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*Solicitors:*
Duncan Cotterill, Nelson
Radich Law, Blenheim

**CIV-2020-442-63**

| | |
|---|---|
| BETWEEN | SPRINGS ROAD PROPERTY LIMITED<br>Plaintiff |
| AND | MICHAEL JOHN MILLAR<br>First Defendant |
| | INVESTMENT SERVICES LIMITED<br>Second Defendant |
| | PAUL JOHN MEPHAN<br>Third Defendant |

**CIV-2020-442-64**

| | |
|---|---|
| BETWEEN | SUPERSTORE PROPERTIES LIMITED<br>Plaintiff |
| AND | MICHAEL JOHN MILLAR<br>First Defendant |
| | INVESTMENT SERVICES LIMITED<br>Second Defendant |

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## Introduction

[1] This is a consolidated claim, brought by each of three related companies which own various commercial properties which they lease to third parties (property companies). The claims are against Investment Services Ltd (ISL), which operates as a commercial property and investment manager; Michael Millar, who is a former director of the plaintiff companies and a director of ISL; and Paul Mephan,[1] who was a director of the property companies for a period between 2018 and 2020.

[2] The plaintiffs' claims relate to fees they say were taken from the property companies, by ISL, in breach of its contract and duty of care, and in breach of Mr Millar's and Mr Mephan's fiduciary and statutory duties owed to the property companies.

[3] The plaintiffs say that each of ISL and Mr Millar has been unjustly enriched by the receipt of a benefit, taken from the property companies. The property companies also plead that Mr Millar knowingly received the plaintiffs' assets in breach of fiduciary obligations owed to them.

[4] The defendants raise a number of counterclaims and affirmative defences.

[5] The proceedings relate to the period 2006 to 2020.

## Background

### *The property companies*

#### *First NZ Properties Ltd*

[6] Foodstore Properties Ltd (which later became First NZ Properties Ltd (First NZ)) was incorporated on 23 August 1995, together with its three subsidiary companies (the subsidiaries) which purchased a supermarket each:

(a) Foodtown Birkenhead;

[1] In CIV-2020-442-62 and CIV-2020-442-63.

(b) Foodtown Blockhouse Bay; and

(c) Foodtown Te Atatu.

(the First NZ Properties).

[7] On 25 September 1995 First NZ and its subsidiaries entered into a Management Agreement with Farmers' Mutual Investment Services Ltd (FMIS) for the investment and property management of the First NZ Properties (the First NZ Management Agreement). At that date, Mr Millar was both a director of First NZ and the Chief Executive Officer (CEO) of Farmers' Mutual Group, FMIS's parent company. At the time of signing, the Agreement was an arm's-length arrangement, there being one independent board member of the First NZ companies.

[8] Also on 25 September 1995, FMIS entered into a Management and Administration Agreement with The Franklin Co Ltd (Franklin), a third party property management company, for Franklin to provide property management services for the First NZ Properties (the First NZ Franklin Agreement). Franklin was paid a management fee of 3.25 per cent of annual gross rentals received.

[9] The last of the First NZ Properties referred to in the First NZ Management Agreement was sold on 4 November 2004.

[10] Further properties were purchased by First NZ: 50 Kilmore Street, Christchurch (Kilmore Street), on 24 December 2003 and 110 Symonds Street, Auckland (Symonds Street) on 31 July 2012.

*Springs Road Property Ltd*

[11] On 2 December 1997 Springs Road Property Ltd (Springs Road) was incorporated and purchased a commercial property at 7 Springs Road, East Tamaki, Auckland (Springs Road Property).

[12] On 13 January 1998 Springs Road entered into a Management Agreement with FMIS for investment and property management (the Springs Road Management

Agreement). At that time, Mr Millar was a director of Springs Road and remained the CEO of Farmers' Mutual Group.

[13] As with First NZ, there was an agreement between ISL and Franklin (entered into on 16 January 1998 by FMIS) for Franklin to perform property management services for Springs Road (the Springs Road Franklin Agreement). Franklin received a fee equivalent to four per cent of the gross rentals received in respect of the Springs Road Property.

*Superstore Properties Ltd*

[14] On 25 January 1999, Superstore Properties Ltd (Superstore) was incorporated. Shortly after, three subsidiary companies each purchased a commercial property (Superstore Properties).

[15] On 9 February 1999, Superstore entered into a Management Agreement with FMIS for investment and property management (the Superstore Management Agreement). Mr Millar was a director of Superstore, and remained the CEO of Farmers' Mutual Group, at the time.

[16] Also on 9 February 1999, FMIS entered into a Management and Administration Agreement with Franklin, for Franklin to provide property management services in respect of the Superstore Properties (the Superstore Franklin Agreement) for a property management fee of three per cent of annual gross rentals received.

***Investment Services Ltd***

[17] ISL was incorporated on 19 June 2000. The initial directors of ISL were Mr Millar and Kenneth Lance Franklin. Mr Millar is currently the sole director of ISL. ISL is owned by the Kaiuma Family Trust. Mr Millar's children are the beneficiaries of the Trust.

[18] FMIS assigned and novated all of its rights, benefits, interests and obligations under the First NZ Management Agreement, the Springs Road Management

Agreement and the Superstore Management Agreement to ISL by deed on or about 12 February 2001. The consideration for the assignment was $200,000 payable, by ISL.

[19] For most of the period the subject of this claim Neil Barnes was the CEO of ISL. Mr Barnes invoiced ISL for his services through his company, Activa Consulting Ltd (Activa). Mr Barnes was also a director of the property companies from 25 June 2001 until 27 February 2018.

[20] Mr Barnes defrauded the property companies of $2,037,946.30. That fraud was disclosed to shareholders after the September 2018 Annual General Meeting. Mr Barnes fled to the United States and, at the time of the hearing in this proceeding, was subject to investigation and prosecution in New Zealand by the Serious Fraud Office. The plaintiffs make some allegations against the defendants in respect of Mr Barnes' fraud. These are discussed at [223] and [290] below.

[21] Mr Millar approached Mr Mephan in or about 2017 to ask if he would be interested in working at ISL. When Mr Barnes stopped working for ISL and the plaintiff companies at the end of February 2018, Mr Mephan took over his duties and responsibilities, assuming the role of CEO. Mr Mephan contracted his services to ISL and the plaintiff companies through his company Corvus Consulting Ltd. Mr Mephan was a director of all three property companies from 13 February 2018 until 21 April 2020. He received no director's fees from those companies. From February 2018 to April 2020, Mr Mephan was CEO of ISL. Mr Mephan was not a director of ISL.

***Property management services***

[22] Franklin provided property management services for the property companies pursuant to the respective Franklin agreements, from the incorporation of each property company until 31 December 2003.

[23] ISL terminated the Franklin agreements on or about 31 December 2003.

[24] From 1 January 2004 ISL employed David Penrose as National Property Manager, effectively an in-house property manager. From April 2007 to August 2010,

Mr Penrose's company Penrose Property Management Ltd (PPML) contracted to ISL to provide property management services.

**[25]** Gravtec Ltd (Gravtec) a company incorporated by Richard Eberlein and Philippa Eberlein, provided property management services to each of the property companies, for First NZ from 1 April 2011 to 31 December 2020; for Springs Road from 1 April 2011 to 31 March 2020; for Superstore from 1 October 2011 to 31 March 2020.

[26] Terra Firma Group Ltd (Terra Firma) provided property management services to First NZ in respect of Symonds Street between 1 April 2012 and 31 March 2020.

***Breakdown of relationship between property companies and ISL***

[27] Mr Mephan resigned as a director of the property companies on 21 April 2020.

[28] Mr Millar resigned as a director of First NZ, Springs Road and Superstore on 7 May 2020. Following a resolution to amend the constitution and allow for shareholders to appoint directors, passed at the September 2020 Annual General Meeting, new directors were appointed. The directors as at the time of this hearing were Damien Prendergast (appointed by Mr Millar from 7 May 2020 and reappointed by shareholders from 28 September 2020) and John Murray (appointed as an independent director from 28 September 2020).

[29] Mr Prendergast and Mr Murray sought independent advice following the possibility of a derivative action being taken by a shareholder and the property companies issued these proceedings in December 2020.

[30] On 31 December 2020 Mr Millar cancelled the First NZ Management Agreement, the Springs Road Management Agreement and the Superstore Management Agreement, alleging that the plaintiff companies had repudiated the agreements.

## Witnesses

[31] Four witnesses gave evidence for the plaintiff companies. Damien Prendergast, a director of the companies, gave evidence about the nature of the companies, their properties, his discovery of the nature of their relationship with ISL, and what occurred subsequently.

[32] John Murray, an independent director and chair of the property companies, appointed in September 2020, gave evidence responding to ISL's counterclaim, in particular the allegation that the property companies' actions amounted to repudiation, entitling Mr Millar to cancel on behalf of ISL.

[33] David Osborn, a forensic accountant, gave expert evidence for the property companies reconstructing payment flows across the property companies and ISL, calculating the amount of the property companies' alleged losses and the gains allegedly received by ISL.

[34] Craig Stobo, an experienced company director, gave evidence about the application of directors' duties to the events in question.

[35] The witnesses for Mr Millar and ISL were:

(a) Mr Millar himself.

(b) David Penrose, one of the professional property managers engaged by Mr Millar to provide property management services to the plaintiffs.

(c) Euan Abernethy, an expert in securities regulation, who discussed the First NZ and Superstore prospectuses and their relevance to the parties' contractual obligations.

(d) Keith Sutton, an expert in corporate governance.

(e) Lorinda Kelly, an expert forensic accountant and chartered accountant, who gave evidence on the extent of the plaintiffs' alleged losses.

[36] Ms Kelly and Mr Osborn also provided a joint statement of experts.

[37] Mr Mephan, the third defendant, gave evidence on his own behalf.

## Overview of First NZ's claims

[38] I deal first with the claims made by First NZ.

### *First NZ Management Agreement*

[39] The stated purpose of the First NZ Management Agreement was to appoint FMIS/ISL as First NZ's agent for the ongoing administration and investment management of First NZ, the subsidiary companies and the identified Properties.

[40] FMIS's duties and responsibilities were:

> **3. DUTIES AND RESPONSIBILITIES OF FMIS**
>
> FMIS shall manage the affairs of FPL and the Subsidiaries, from the date of this Agreement, including without limitation:
>
> 3.1 attend to all matters necessary or desirable in relation to the Offer, including the preparation of the prospectus, promotion of the Offer, procurement of an underwriter, payment of brokerage and processing of applications;
>
> 3.2 arrange finance for their activities from such sources and on such terms and conditions as to security or otherwise as FMIS in consultation with FPL and the Subsidiaries deems fit;
>
> 3.3 procure and supervise the acquisition, management and eventual sale of the Properties with the assistance of a professional property manager;
>
> 3.4 arrange the management of FPL's share register and the payment of all distributions;
>
> 3.5 arrange for the issue of share certificates and the operation of the secondary market for FPL's shares;
>
> 3.6 procure the filing of all returns for FPL and the Subsidiaries with the Inland Revenue Department and the Companies Office;
>
> 3. 7 arrange for the preparation and audit of such financial statements and accounts as FPL and the Subsidiaries are required by any statute to prepare and have audited;
>
> 3.8 operate all bank accounts;
>
> 3.9 instruct such solicitors, accountants, auditors, valuers or other consultants or advisers as FMIS deems necessary or desirable in connection with any of its duties and responsibilities under this Agreement;

> 3.10 do or perform any other act or thing which FPL or a Subsidiary may reasonably request in connection with the investment and administrative management of FPL, the Subsidiaries, and the Properties.
>
> …

[41] The First NZ Management Agreement provided that, in "consideration of the performance by FMIS of its duties and responsibilities under this Agreement" it would receive a management fee of 3.25 per cent per annum of gross rentals received in respect of the Properties, for an initial period to 31 March 1996. Thereafter, FMIS was to be paid an "annual management fee" of 6.50 per cent per annum of annual gross rentals until termination of the Agreement.

[42] From the time the First NZ Management Agreement was entered into, until termination of the First NZ Franklin Agreement, the cost of property management was met from within the management fee paid to FMIS/ISL[2] under the First NZ Agreement.

[43] ISL terminated the First NZ Franklin Agreement on or about 31 December 2003.

[44] After the First NZ Franklin Agreement was terminated, ISL appointed an in-house property manager to manage the First NZ Properties. Mr Penrose and his company PPML provided those property management services until October 2011. Mr Penrose and PPML's fees were met from within the management fee.

[45] The essence of First NZ's claim is that following termination of the First NZ Franklin Agreement ISL charged First NZ, and First NZ paid ISL, amounts additional to the management fee, allegedly for the provision of property management services, without authorisation or agreement.

[46] In total, the amounts First NZ says it paid were:

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[2] As noted at [18] above, FMIS's rights under the Management Agreement were assigned to ISL on 12 February 2001.

(a) ISL $1,159,081.00 plus GST, being 3.25 per cent of gross rentals, as a property management fee, pursuant to the First NZ Management Agreement ("property management"/"disclosed fees"); and

(b) ISL $183,220 plus GST ($15,000 per month) also for property management ("excess fees"); and

(c) Gravtec $204,328.87 plus GST ($22,000 per annum), for property management services; and

(d) Terra Firma $203,143.86 plus GST ($30,000 per annum) for property management services for Symonds Street.

[47] First NZ further claims that ISL directed payment to itself of gain fees, totalling $830,000, on the sale of two First NZ properties, to which it had no entitlement.

[48] First NZ says the payments listed at [46] and [47] above were made with the knowledge, and at the direction of, Mr Millar who was at all times a director of both First NZ and ISL and, between 13 February 2018 and 31 March 2020, with the knowledge, and at the direction of, Mr Mephan. First NZ's various claims are framed in breach of fiduciary duty (Mr Millar and Mr Mephan), breach of ss 131 and 137 of the Companies Act 1993 (Mr Millar and Mr Mephan), unjust enrichment (Mr Millar and ISL), knowing receipt (Mr Millar), and breach of contract and negligence (ISL).

**Preliminary interpretation questions**

[49] First NZ's claims raise two significant questions: first, what were ISL's obligations and entitlements under the First NZ Management Agreement? In particular, what did the 6.50 per cent management fee encompass? Second, when did the First NZ Management Agreement come to an end and what were the terms of the agreement between First NZ and ISL after the sale of the last of the First NZ Properties?

***What were ISL's obligations and entitlements under the First NZ Management Agreement?***

[50] First NZ says that at all relevant times it paid ISL a management fee of 6.50 per cent of annual gross rentals of the First NZ Properties.

[51] Mr Osborn gave evidence for the plaintiffs of the manner in which Franklin was paid while it was First NZ's property manager (up to 31 December 2003). Franklin collected the gross rentals from the tenants, deducted its 3.25 per cent property management fee, then passed the remaining rental income to First NZ. First NZ then paid the remainder of the 6.50 per cent management fee to ISL.

[52] First NZ says that is how ISL complied with the contractual obligation to "procure and supervise the acquisition, management and eventual sale of the Properties with the assistance of a professional property manager". It says those undisputed arrangements illustrated the proper contractual arrangement between First NZ and its property manager. That is demonstrated by the performance of the contract from 1995 to the end of 2003. Some of ISL's own working documents referred to the "Property Management Fee" as 3.25 per cent.

[53] In support of its interpretation First NZ also relies on a statement in the 5 October 1995 prospectus issued by the Farmers' Mutual Group, for Foodstore Properties Ltd. The prospectus explained the arrangement under the First NZ Management Agreement as being:

> (a) FMIS ("Investment Manager") was responsible for the investment management of First NZ, including promotion, financial management and ongoing administration.
>
> (b) The Investment Manager was to receive (after 31 March 1996) an investment management fee of 6.50 per cent of annual rental income payable monthly in arrears.
>
> (c) Franklin ("Property Manager") would provide independent and operational property management services in respect of the Properties.

(d) The ongoing property management fee shall be borne by the Investment Manager, out of the investment management fee.

[54] First NZ says that nothing changed in the eight years following signing of the First NZ Management Agreement on 25 September 1995 to justify any change in the way the terms of the Agreement applied and, in particular, nothing would have justified ISL treating the 6.50 per cent annual management fee as being solely for investment management.

[55] The defendants argue that ISL's obligation under the First NZ Management Agreement was to "supervise" management of the plaintiffs' property, with the assistance of a professional property manager. ISL was entitled to engage an external property manager on First NZ's behalf, to be paid by First NZ in addition to the 6.50 per cent management fee paid to ISL under the Agreement.

[56] That supervision was carried out with the assistance of a professional property manager from the outset, initially Franklin. While the defendants agree that Franklin's fees were met from the management fee to which ISL was entitled under cl 11.1(c) of the Agreement, that was not required by the Agreement. They say there was no allocation of the fee to 50 per cent for investment management and 50 per cent for property management as First NZ submits. By way of example, they point to two invoices rendered by ISL to First NZ which refer to the "management fee" of 6.50 per cent.

[57] The defendants rely on cl 3.9 of the First NZ Management Agreement, in combination with cl 4.1. Clause 3.9 provides:

> FMIS shall manage the affairs of FPL and the Subsidiaries, from the date of this Agreement, including without limitation:
>
> …
>
> 3.9 instruct such solicitors, accountants, auditors, valuers or other consultants or advisors as FMIS deems necessary or desirable in connection with any of its duties and responsibilities under this Agreement;

[58] Clause 4.1 states:

> In performing its duties and responsibilities under this Agreement, FMIS shall act solely as the agent of FPL and the Subsidiaries. All costs, disbursements, expenses, taxes, debts and liabilities to third persons incurred by FMIS in the performance of its duties and responsibilities under this Agreement shall be the costs, disbursements, expenses, debts and liabilities of FPL and the Subsidiaries (as relevant) only and FMIS shall not be liable for any such obligation by reason of performance of its duties and responsibilities under this Agreement.

*Discussion*

[59] I accept the plaintiffs' submission that, in the context of the First NZ Management Agreement as a whole, cl 3.9 of the Agreement cannot be construed to include a property manager within the category of "other consultants or advisors", when cl 3.3 specifically refers to "professional property managers". The general principles of interpretation apply so that the specific prevails over the general.[3]

[60] Nor do I accept the defendants' interpretation of cl 4.1 of the Agreement. Clause 4.1 is a boilerplate clause, recognising the agency function that FMIS/ISL would be carrying out for First NZ. The purpose of that clause is to protect ISL from being held liable to third parties separately as a principal. It is predicated on ISL as agent properly incurring a liability to a third party. It does not apply to ISL's first party liability to First NZ if it acts outside the terms of their agreement.[4]

[61] The First NZ Management Agreement did not specifically divide the "annual management fee" of 6.50 per cent per annum of annual gross rentals into "property management" and "investment management" components. Nevertheless, the practice under the agreement, from September 1995 to December 2003, when the First NZ Franklin Agreement was terminated, was that 3.25 per cent of the fee was applied by ISL to property management. That is accepted by the defendants. The high point of their argument is the two invoices that refer to the management fee of 6.50 per cent. That is not of much assistance — the management fee as a whole was 6.50 per cent, the question is what it encompassed.

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[3] See for example Kim Lewison *The Interpretation of Contracts* (8th ed, Sweet & Maxwell, London, 2024) at [7.46].

[4] Ian Gault (ed) *Gault on Commercial Law* (online ed, Thomson Reuters) at 19.5.2.

[62] The defendants also say that the purchase of new properties by First NZ necessitated different arrangements from those in place when Franklin was providing property management services. But as I discuss later, the defendants did not at any point specifically raise with First NZ that it proposed to change the arrangement that existed under the Franklin Agreement and treat the 6.50 per cent annual management fee as being solely for investment management.

[63] The prospectus relied on by First NZ post-dates the First NZ Management Agreement by 10 days and therefore, the defendants say, cannot be called in aid by First NZ.

[64] In *Bathurst Resources v L&M Coal Holdings Ltd*,[5] the Supreme Court considered the admissibility of extrinsic material of surrounding circumstances both before and after the execution of the relevant contractual documents.

[65] In relation to the parties' conduct in undertaking their contractual obligations after entering into the contract, the Court concluded (agreeing with the approach of Tipping J in *Wholesale Distributors Ltd v Gibbons Holdings Ltd*[6]) that the approach to the admissibility of subsequent conduct should be the same as the approach to the admissibility of prior negotiations.[7] The Court also cited Tipping J's later refinement of this approach in *Vector Gas*, where he said:[8]

> [31] There is no logical reason why the same approach should not be taken to both post-contract and pre-contract evidence. The key point is that extrinsic evidence is admissible if it tends to establish a fact or circumstance capable of demonstrating objectively what meaning both or all parties intended their words to bear.

[66] In *Bathurst* the Court said "the court must ask itself whether the subsequent conduct tends to prove anything relevant to the objective approach to interpretation."[9]

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5 *Bathurst Resources Ltd v L&M Coal Holdings Ltd* [2021] NZSC 85, [2021] 1 NZLR 696.
6 *Wholesale Distributors Ltd v Gibbons Holdings Ltd* [2007] NZSC 37, [2008] 1 NZLR 277.
7 *Bathurst Resources Ltd v L&M Coal Holdings Ltd*, above n 5, at [89].
8 At [88], quoting *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC 5, [2010] 2 NZLR 444 at [31].
9 *Bathurst Resources Ltd v L&M Coal Holdings Ltd*, above n 5, at [89].

[67] Here, the prospectus was plainly proximate to the Agreement (issued some 10 days later). Farmers' Mutual Group issued the prospectus. Mr Millar was CEO of Farmers' Mutual Group at that point. The directors of Foodstore Properties Ltd (later First NZ) at that time were Mr Millar, Mr Barnes and Virginia Laughton. It is mutual in that both parties to the Agreement must have been aware of it, and having regard to Mr Millar's roles in each of Farmers' Mutual Group and Foodstore Properties/First NZ (although the Supreme Court said the subsequent conduct need not necessarily be mutual[10]).

[68] While of course it is not determinative, the statement in the prospectus is relevant to the question how the payment arrangement under the First NZ Management Agreement should be interpreted and it is consistent with the practice for the first eight years of the Agreement and the interpretation now advanced by First NZ.

[69] In conclusion, as the Supreme Court put it in *Bathurst*,[11] the term to be implied arises from the text of the contract, interpreted against the relevant background.

[70] I find that the First NZ Management Agreement required the cost to ISL of engaging a property manager was to be funded from the property management fee paid by First NZ to ISL.

[71] The consequence of that interpretation is that ISL is not entitled to claim the management fee under the Agreement and a separate amount to pay itself and/or an external property manager for property management services. That is discussed further below in relation to First NZ's specific claims.

***When did the First NZ Management Agreement come to an end?***

[72] First NZ says that the very purpose of the Management Agreement was the First NZ Properties (being the entirety of First NZ's business). Those properties are specifically defined in the Schedule to the Agreement:

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10 At [89]

11 At [115].

**SCHEDULE**

1. Description of the Properties:

Foodtown Blockhouse Bay
19-29 Donovan Street
(to be acquired and owned by
Foodstore Properties (Blockhouse
Bay) Limited

Foodtown Birkenhead
180 Mokoia Road
(to be acquired and owned by
Foodstore Properties (Birkenhead)
Limited)

Foodtown Te Atatu
Edmonton Road and Te Atatu Road
(to be acquired and owned by
Foodstore Properties (Te Atatu)
Limited)

[73] The Agreement did not refer to the acquisition of any additional or replacement properties. After the sale of the last property, ISL no longer had any duties or responsibilities in respect of the Properties, nor were any management fees payable because there was no longer any rental income being received in respect of the First NZ Properties.

[74] Accordingly, First NZ says, the Management Agreement came to an end when the last of the Properties (Foodtown Te Atatu) was sold on 4 November 2004. At that point, the purpose of the Agreement was exhausted.

[75] First NZ says that after sale of the Te Atatu property, ISL, as evidenced by its conduct, made an offer to First NZ to consider providing investment and property management services. First NZ accepted that offer and a new, unwritten, agreement took the place of the Agreement; it was not simply a variation or amendment of the initial Management Agreement. The new contract was entered into in or around November 2004.

[76] First NZ's submission is that, as under the First NZ Management Agreement, the new agreement provided for a payment to ISL of a management fee of 6.50 per cent of annual gross rentals. The new agreement covered subsequently acquired properties and provided that 3.25 per cent of annual gross rentals (that is 50 per cent of the total 6.50 per cent management fee) was to be applied by ISL to property management of the subsequently acquired properties. That new contract continued for some 15 years.

[77] First NZ urges the adoption of a broader approach, "considering objectively the totality of the parties' dealings to determine whether a concluded bargain has been reached".[12]

[78] The first and second defendants in response say that the First NZ Management Agreement continued following the sale of the last of the three original First NZ Properties and applied to the subsequent acquisition by First NZ of further properties.

[79] The defendants point out that the First NZ Management Agreement did not have a fixed term, nor did it provide that it would expire on the sale of the last of the original Properties.

[80] Mr Millar's evidence was that neither First NZ nor ISL considered the agreement to have terminated after the sale of the last First NZ Property. Following the sale, ISL was to continue managing any replacement properties purchased by First NZ on the basis that the Management Agreement was continuing.

[81] Mr Millar said:

> … both parties were operating on the basis that the management agreement was, despite the sale of the last original property, continuing and neither party considered the agreement to have terminated.

[82] The defendants also note that the directors of First NZ sought shareholder approval by way of special resolution to purchase a "replacement property" following the sale of the last of the original Properties. The shareholders did authorise the purchase of a replacement property and, by extension, the continued management of

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12 Gault, above n 4, at [CC2.01].

that property by ISL on the terms and conditions in the First NZ Management Agreement. The shareholders' approval of the purchase of a replacement property is evidence that the shareholders also accepted that the term "Property" in the management agreement would apply to the replacement property.

[83] The defendants rely on *CSR Ltd v Adecco (Australia) Pty Ltd*.[13] In that case a formal contract for the supply of labour between Adecco and CSR had expired. Under the contract, Adecco was liable to indemnify CSR against personal injury suffered by temporary staff. After the agreement expired, Adecco continued to supply labour, and CSR continued to pay at the same price as in the expired contract. The New South Wales Court of Appeal held that, following expiry of the agreement, the parties' continued conduct gave rise to an implied contract on the expired terms, including the indemnity provision.

[84] The defendants say that is the situation here — First NZ continued to own property and ISL continued to provide property management services, under a new contract, on the terms of the First NZ Management Agreement.

[85] The third defendant submits that the parol evidence rule applies, with the consequence that any evidence from the plaintiffs to establish the existence of a new, undocumented arrangement between First NZ and ISL is inadmissible.

*Discussion*

[86] First I address the discussion about the parol evidence rule.

[87] I accept the submission for First NZ that it did not in fact adduce any evidence to suggest that the First NZ Management Agreement was added to, varied or contradicted in any way. It says there was no related party transaction approval, no disclosure in the interests register, and no other corporate documentation suggesting there was an amendment. First NZ says it was a new agreement.

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13 *CSR Ltd v Adecco (Australia) Pty Ltd* [2017] NSWCA 121. See also *Andar Transport Pty Ltd v Brambles Ltd* [2002] VSCA 150.

[88] In addition, as First NZ notes, the relevance of the parol evidence rule has greatly diminished, as a consequence of the Evidence Act 2006, which largely codifies the rules of admissibility.[14] In the *Bathurst* case the Supreme Court held that it is well-settled that the parol evidence rule does not govern the admissibility of extrinsic material in relation to contractual interpretation and the correct approach is to start with the Evidence Act to determine the admissibility of all evidence in court proceedings.[15]

[89] In *Bathurst*, the Supreme Court described the proper approach to contractual interpretation as an objective one, the aim being to ascertain:[16]

> … the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

[90] At first blush the interpretation advanced by the plaintiffs is not completely consistent with the wording of the Agreement. For example, in the Introduction to the Agreement, cl D states:

> FPL [Foodstore Properties Ltd] and the Subsidiaries wish to appoint FMIS as their agent for the ongoing administration and investment management of FPL, the Subsidiaries and the Properties, and FMIS wishes to accept such appointment, on the terms and conditions set out in this Agreement.

[91] That wording is largely repeated in cl 1 of the Agreement. The wording suggests that the purpose of the Agreement is broader than the management of the named Properties. That is, it also covers the ongoing administration and investment management of Foodstore Properties Ltd and its subsidiaries.

[92] On that view, in the absence of a terminating event in terms of cl 17, the Agreement would have continued on foot, because its ambit was broader than the First NZ Properties.

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14 Helen Winkelmann, Susan Glazebrook and Ellen France "Contractual Interpretation" (2020) 51(3) VUWLR 463 at 504.

15 *Bathurst Resources Ltd v L&M Coal Holdings Ltd*, above n 5, at [56]–[58].

16 At [41], quoting *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 (HL) at 912.

[93] However (apart from an establishment and administration fee) ISL's remuneration under cl 11 of the Agreement is framed solely in terms of fees in relation to the Properties. First, a management fee in respect of the Properties up until 31 March 1996; second, an annual management fee, based on annual gross rentals, thereafter; and third, a proportion of any capital gains on the sale of any of the Properties.

[94] ISL's ongoing fees were dependent on there being at least one property to generate the gross rentals. "Gross rentals" is defined (in cl 11.2) as:

> means all rental premiums, licence fees, monies received from or in respect of any loss of profits pursuant to an insurance policy or policies and all other income whatsoever received in respect of the Properties…

[95] The Properties are set out in the Schedule and described at [72] above.

[96] The Agreement related to the Properties as defined. Once the Properties were sold, the terms of the Agreement no longer applied, even though the termination provisions were not invoked.

[97] While the plaintiffs in this case sought to distinguish *CSR v Adecco* on the basis that it arose in an employment context, I think the defining feature of *CSR* for the purpose of this case is that it involved the implication of a new contract, on the expired terms, as between two arms-length parties. That was not the case here.

[98] The question in this case is whether the Court can "conclude with confidence"[17] that the conduct of the parties signalled consent to an ongoing arrangement on the old terms.

[99] It is clear that there was no express intention or consent from First NZ. Mr Millar says neither party considered the agreement to have expired and both parties were operating on the basis that the same terms continued to apply.

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[17] *Blackpool and Fylde Aero Club Ltd v Blackpool Borough Council* [1990] 3 All ER 25 at 31.

[100] But, as Mr Millar conceded in cross-examination, "neither party" meant Mr Millar, wearing his ISL director hat, on the one hand, and his First NZ director hat, on the other. The other two directors of First NZ at the time of the sale of the last of the Properties were Mr Millar's employees, Ms Laughton and Mr Barnes. There were no independent directors.

[101] Mr Millar could not recall whether he had considered, in his capacity as a director of the plaintiffs, whether it was in the best interests of First NZ to continue with the First NZ Management Agreement. Nor was the question of continuation of the Management Agreement specifically put to shareholders, either at the point of sale of Foodtown Te Atatu or when shareholder consent was sought to purchase a new property. The 25 June 2003 letter to shareholders (signed by Mr Millar) inviting attendance at the Extraordinary General Meeting to vote on the acquisition of a new property did not address the ISL/First NZ management arrangements.

[102] In addition, it was plainly in ISL's business interests to continue as if it were business as usual. As Mr Mephan acknowledged in cross-examination, the plaintiffs comprised between 50 and 75 per cent of ISL's business.

[103] Nor can it be said that it was necessary for business efficacy or so obvious that it goes without saying[18] that the terms argued for by defendants be implied. One commentator has observed[19] that in *Andar Transport Pty Ltd v Brambles*,[20] the continuing relationship between the parties was inexplicable, absent the expired terms.

[104] In this case there was no evidence specifically directed at what specific terms were necessary for business efficacy, but there must have been a practical possibility that if the situation had been brought to the attention of First NZ in a clear and independent way, it may well have sought to exclude any ongoing provision for gain fees and would likely not have agreed to a practical increase in the management fee.

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18 The second and third of the five conditions for implication of a term set out by the Privy Council in *BP Refinery (Westernport) Pty Ltd v President, Councillors and Ratepayers of the Shire of Hastings* (1977) 180 CLR 266 (PC) at 283.

19 Ben Sears "Implied contract? When conduct continues after a contract expires" (LLB research paper, Victoria University of Wellington, 2022).

20 *Andar Transport Pty Ltd v Brambles Ltd*, above n 13.

[105] In those circumstances, it is not possible to imply a continued contract on the terms argued for by the defendants.

[106] I conclude that the First NZ Management Agreement was solely for the purpose of the Properties and came to an end on the sale of the last of the Properties.

[107] Nevertheless, plainly, and as the parties agree, there was a further management agreement between them after the sale of the last of the First NZ Properties in November 2004. ISL continued to provide property management services for subsequently acquired properties and First NZ continued to pay ISL.

[108] I conclude that continuation of a contract between First NZ and ISL was on the basis of ISL continuing to be paid a total management fee of 6.50 per cent of annual gross rentals, which was to cover both "investment management" and "property management", as had been the case while Franklin was engaged as property manager. I also accept First NZ's submission that the new agreement did not provide for the payment of gain fees on the sale of any further-acquired properties. This is discussed further at [176]–[185] below.

**First NZ's claims**

[109] The specifics of First NZ's claims are set out below.

***Disclosed property management fee***

[110] From 1 April 2005 to 31 March 2021 ISL received from First NZ a property management fee of $1,159,00.81 plus GST. This was 3.25 per cent of gross rentals, being the property management fee. First NZ characterises the $1,159,00.81 plus GST as the "disclosed property management fee".

[111] The First NZ agreement with Franklin came to an end on or about 31 December 2003. ISL then took the property management function "in-house", engaging David Penrose, and then PPML, as property manager.

[112] The cost to engage Mr Penrose to provide property management services in-house was a fraction of the cost of engaging Franklin: for example, for the financial year ending 31 March 2007, the cost of property management recorded in the general ledger was $9,500. The disclosed management fee was $94,530. 50 per cent of that amounted to $47,265.

[113] Notwithstanding that, FNZ says there was no review on termination of the First NZ Franklin Agreement and bringing the property management function in-house, of what would be in First NZ's best interests.

[114] The plaintiffs say that there is no evidence that Mr Millar, as director of First NZ, ever considered whether continuing to charge a property management fee at 3.25 per cent would be in the best interests of First NZ. Rather, he allowed a situation where, on termination of the First NZ Franklin Agreement, ISL was immediately able to increase its earnings from the First NZ Management Agreement.

[115] First NZ purchased the Kilmore Street property in December 2003. Kilmore Street had multiple tenants and therefore an operating expenses (Opex) management account. First NZ says that ISL continued to receive the 3.25 per cent property management fee, where that fee was effectively being met by the tenants of the First NZ properties and made no reduction to First NZ. In doing so, Mr Millar and Mr Mephan (from 13 February 2018 to 31 March 2020) profited in breach of their fiduciary and statutory duties to First NZ.

[116] In summary, First NZ paid ISL the entire management fee when at the same time the actual costs of property management were significantly less than were incurred by ISL.

[117] First NZ seeks recovery of an amount equal to half of 6.50 per cent of the annual gross rentals paid to ISL from 1 April 2005 to 31 March 2021.

*"Excess" property management fees*

[118] In the period 1 April 2006 to 31 March 2020, First NZ paid to ISL an "Opex management" fee of $183,220.00 plus GST, characterised by First NZ as undisclosed "excess" property management fees.

[119] It says this amount was paid by way of monthly automatic payments from First NZ to ISL and it was "excess" in that it was charged in addition to the 3.25 per cent property management fee.

[120] First NZ says that ISL was not entitled to charge First NZ fees for property management services that it did not perform and that were already part of the management fee being charged to and paid by First NZ.

[121] First NZ says there was no contractual basis for the payments.

[122] Where a property was tenanted the tenants were charged an amount equivalent to the excess fees, as Opex. First NZ says that where Opex was received from the tenants it did not retain those amounts, but paid them to ISL.

[123] Mr Osborn's evidence for the plaintiffs was that the Opex charges were not revealed in the Annual Reports for each of the plaintiff companies, because the charges and their payment by tenants net to an overall nil figure. Mr Osborn observed that there is no reporting of the excess property management fees as a line item, nor of the receipts from tenants. The excess fees were paid regardless of whether the relevant property was tenanted and Opex paid.

[124] Mr Millar accepted that there was no contract for fees to be paid by First NZ to ISL over and above the 6.50 per cent management fee, but agreed that ISL did in fact receive these, additional payments.

[125] The defendants' response is that the "excess" fees were for legitimate services provided to First NZ by ISL, additional to the services it was obliged to provide under the Management Agreement. The defendants say that the fees were in fact not for property management, but for "Opex management". The Opex management services

provided by ISL were services previously provided by Franklin and which neither of the third party professional managers subsequently appointed (Gravtec and Terra Firma) were in a position to provide. These services were therefore in addition to the management services provided by ISL to First NZ in terms of the First NZ Management Agreement.

[126] As to the allegation that the fees were undisclosed, the defendants rely on s 140(2) of the Companies Act to submit that general disclosure of the payments was sufficient. This took the form of general disclosure in all annual accounts that all transactions between First NZ and ISL were related party transactions and transactions in which Mr Millar had an interest.

[127] Second, they were recorded in general terms — that Mr Millar was personally interested in transactions between First NZ (and Springs Road) on the one hand and ISL on the other — in the companies' interest registers, in all relevant periods.

[128] Further, although Mr Millar was an interested director, he was able to approve the fees because the First NZ Constitution specifically provides that an interested director is able to authorise transactions in which he or she has an interest.

[129] The defendants agree that the "excess" fees did not appear in the annual accounts of First NZ, but say this was not a failure of disclosure in accounting terms (although this was not pleaded). The fees do not appear in the annual accounts because they were not revenue, costs or expenses of First NZ and had no bearing, positive or negative, on the equity position of First NZ which is required to be described in the annual accounts.

[130] Accordingly, the fees cannot be said to be "undisclosed" in breach of the defendants' obligations.

***Directing payments to Gravtec and Terra Firma***

[131] First NZ also claims in respect of payments made to third party property managers Gravtec and Terra Firma. In respect of both First NZ says the payments were made with the knowledge, and at the direction, of Mr Millar and Mr Mephan (in

the period 13 February 2018 to 31 March 2020) in breach of their fiduciary and statutory duties.

*Gravtec*

[132] Between 1 April 2011 and 31 December 2020, First NZ paid Gravtec fees of $204,328.87 plus GST for property management services. It is common ground that Gravtec's fee was not met from within the 3.25 per cent property management fee. First NZ also says the payments to Gravtec were not disclosed by ISL.

[133] The defendants rely on an agreement between Gravtec and First NZ as the legal basis for the payments to Gravtec. That agreement (signed by Mr Barnes for First NZ) is dated 20 November 2017, but stated to commence on 1 October 2011.

[134] First NZ submits that Mr Millar's explanation for the backdating — in essence, to minimise the risk of Mr Barnes "causing difficulty" on his termination — lacks credibility and was an artifice. In addition, the Gravtec agreement was not disclosed to First NZ shareholders until the 2020 Annual Report. Again, First NZ submits that Mr Millar's explanation for this — that it was not intentionally disguised but was a matter of "property administration" — lacks credibility.

*Terra Firma*

[135] Between 1 April 2012 and 31 March 2020, First NZ paid Terra Firma fees of $203,143.86 plus GST for the provision of property management services for First NZ's property at Symonds Street. As with Gravtec, the fees to Terra Firma were paid by First NZ in addition to the management fee paid to ISL and in addition to the "excess" property management fees.

[136] The defendants rely on an agreement between First NZ and Terra Firma as the legal basis for the payments to Terra Firma. The agreement is undated, states that it relates to "a period expiring on 31 March 2019", but does not have a start date. Mr Mephan signed that agreement on behalf of First NZ and confirmed that it was likely signed on or about March 2018.

[137] First NZ alleges that, as with Gravtec, the engagement of Terra Firma was to fulfil a function for which ISL was already receiving a fee from First NZ and was, in addition, receiving Opex management fees from the tenants of the properties.

[138] First NZ also say the existence of the agreement and payments to Terra Firma were not disclosed to First NZ's shareholders — they were not mentioned in the annual accounts. Mr Sutton, in his evidence for the defendants as an expert in corporate governance, acknowledged that the agreement and payments were not in plain sight.

[139] Mr Millar accepted that the property management services provided by Gravtec, and subsequently Terra Firma, were a subset of the services that were being provided by ISL to First NZ.

[140] Mr Millar also accepted that First NZ's shareholders would not have been aware of the backdated contract with Gravtec.

[141] But the defendants say that the payments were for legitimate property management services for which First NZ had an obligation to pay. ISL had a contractual entitlement to the management fee of 6.50 per cent of annual gross rentals. In addition, the Management Agreement gave ISL power to "instruct such … consultants or advisers as [ISL] deems necessary or desirable in connection with any of its duties and responsibilities under this Agreement". It relies on cl 4.1 of the Agreement to submit that the costs incurred in doing so are First NZ's costs.

[142] The payments were for legitimate services, actually provided by Gravtec and Terra Firma. Further, the costs of engaging Gravtec and Terra Firma were incurred by the tenants, by way of Opex, and not by First NZ, therefore there was no loss to First NZ.

[143] Mr Millar, Mr Mephan and ISL did not benefit from the payments to Gravtec and Terra Firma — none of them has any interest in those companies.

[144] The defendants also submit that there was no obligation to disclose the Gravtec and Terra Firma agreements and payments to First NZ's shareholders because the payments were not a cost, expense or revenue of First NZ.

***Gain fees***

[145] In addition to the fees for property management, First NZ also seeks to recover gain fees paid to ISL:

(a) $380,000 plus GST for 50 Kilmore Street. The full gain fee charged was $430,000 plus GST. However, $50,000 plus GST has been recovered from Mr Barnes as part of the fraud recovery; and

(b) $450,000 plus GST for 110 Symonds Street.

[146] The First NZ Management Agreement provided for the payment of gain fees of five per cent of any capital gains realised on the sale of First NZ Properties. But First NZ says there was no contractual or other entitlement for the payment to ISL of the gain fee on either of the Kilmore Street or Symonds Street properties. Clause 11.1(d) of the First NZ Management Agreement (the gain fees provision) did not apply at all to either property, or any other property which was not one of the Properties described in the Schedule to the First NZ Management Agreement. (In any event, it says, Kilmore Street was not "sold").

[147] Nor is there any evidence that the parties intended for, or provided any consideration for, the claiming of a gain fee on the sale of a replacement property for the Properties.

[148] First NZ also relies on the introduction to the First NZ Management Agreement which explains that each of the subsidiary companies intends to purchase a specific property. Each property is defined as a "Property" and together they are defined as the "Properties". The Agreement does not refer to any intention to purchase additional properties, or to the payment of fees if additional properties are purchased. The payment provision, and the First NZ Management Agreement as a whole, refer expressly to the "properties" only.

[149] First NZ points to the First NZ prospectus of 5 October 1995, to support this submission. The prospectus refers only to the Properties. The Chairman's letter refers to the "ownership of the premises of three suburban Auckland supermarkets, Foodtown Te Atatu, Foodtown Blockhouse Bay, and Foodtown Birkenhead." It goes on to say:

> Foodstore Properties Limited has been developed specifically to allow investors to participate in the attractive income flows generated from these properties as well as any capital growth that may be realised from their eventual sale.

[150] Clause 3 of the First NZ Management Agreement states that ISL shall manage the affairs of First NZ and the Subsidiaries, including the "acquisition, management and eventual sale of the Properties" and shall do any act or thing reasonably requested by First NZ or a Subsidiary". First NZ says this supports the view that the First NZ Management Agreement is focused on acquisition and management of the Properties only.

[151] First NZ says that ISL had no contractual or other entitlement to the gain fees. In respect of the Kilmore Street gain fee, Mr Millar, and in respect of the Symonds Street gain fee, Mr Millar and Mr Mephan, breached their fiduciary and statutory duties owed to First NZ by directing the payment of the gain fees:

(a) when it was not in the best interests of First NZ;

(b) where there was a failure to exercise due care and skill to establish an obligation on the part of First NZ to make the payment; and

(c) where there was no proper contractual basis to do so.

[152] By directing the payment of the gain fees, Mr Millar (in the case of Kilmore Street) and Mr Millar and Mr Mephan (in the case of Symonds Street) profited at the expense of First NZ.

[153] The defendants rely on the terms of the First NZ Management Agreement which provided, at cl 11.1(d) that Foodstore Properties Ltd (First NZ) agreed to pay to

FMIS (ISL) "5.0 per cent of any capital gains realised on the sale of any of the Properties."

[154] The defendants say that the First NZ Management Agreement, including the provision relating to payment of a gain fee, did continue in effect after the sale of the three Properties named in the Schedule and cl 11.1(d) should be construed as applying to the sale of any subsequently acquired properties. By way of example, Mr Millar gave evidence of the First NZ shareholders approving the purchase of a new property. On that basis ISL was entitled to the payment of both the Kilmore Street and Symonds Street gain fees.

[155] The parties' experts accepted that the gain fees had been correctly calculated, however Ms Kelly, for the defendants, identified an error in the calculation of the fee in the amount of $15,630, in relation to Kilmore Street. The first and second defendants accept an obligation to repay this amount.

*Kilmore Street*

[156] Mr Millar directed the payment of a $430,000 plus GST gain fee from First NZ to ISL in 2012.

[157] The Kilmore Street gain fee was paid in two tranches. First, $280,000 plus GST, on 11 June 2012, for an "interim fee for capital gain following the settlement of the Material Damage claim on Kilmore Street". Second, $150,000 plus GST on 17 August 2012 for the "Balance of fee for capital gain following sale of the Kilmore Street land". ISL did not receive the entire gain fee as $50,000 (plus GST of $7,500) was paid fraudulently to the company Activa. For that reason First NZ seeks to recover only $380,000 in this proceeding.

[158] First NZ says the Kilmore Street gain fee was not disclosed in any annual accounts as a related party transaction. As acknowledged by Ms Kelly for the defendants, it was not included as part of the Management Fee reported in the 2013 annual accounts. First NZ says that it is disguised by the reporting of the proceeds of the disposal of the property as a net figure.

[159] First NZ says that even if the First NZ Management Agreement did apply to allow payment of a gain fee, there was no "sale" of Kilmore Street. The Kilmore Street property suffered damage in the Christchurch earthquakes of 2010 and 2011. In 2012 Foodstore (Cranmer) Ltd (a wholly owned subsidiary of First NZ) settled an insurance claim in respect of damage to the building for $12,600,000 plus GST and sold the bare land for $3,000,000 plus GST.

[160] Mr Millar's evidence covers what happened to Kilmore Street as a result of the September 2010 and February 2011 earthquakes. Some repair work was necessary after the first earthquake. ISL took responsibility for First NZ's obligations as landlord of the property and organised some repair work, liaising with tenants, the insurance company and the professionals responsible for the repairs. Shortly before tenants were due to move back into the building the second, February, earthquake struck. ISL again took responsibility, as First NZ's agent, to obtain expert reports about the structural integrity and safety of the building. The cost of carrying out the experts' recommendations for keeping the building stable was significant and the insurance company would not commit to the cost of the repairs. A settlement was negotiated with the insurance company which resulted in a payment to First NZ of $12,600,000 plus GST. The building was then demolished and the bare land was sold for $3,000,000 plus GST. ISL was responsible for negotiating the insurance settlement and the sale of the land, Mr Millar said at considerable effort, for an ultimate pay-out to First NZ of the insurance proceeds and, later, the sale of the bare land.

[161] Mr Millar's evidence is that ISL considered it was entitled to a gain fee in relation to the insurance proceeds under the First NZ Management Agreement because of the transaction with the insurance company being a "deemed sale". ISL took a gain fee on the basis of the difference between the building and the bare land acquisition values and the sales. It invoiced First NZ for a gain fee totalling $430,000 plus GST.

*Symonds Street*

[162] The multi-storey property at 110 Symonds Street, Auckland was purchased (through First NZ's 100 per cent-owned subsidiary Symonds 110 Ltd) from the

remaining proceeds of the insurance settlement on Kilmore Street. It was sold in 2018. A gain fee of $450,000 on the sale was paid to ISL, on 20 November 2019.

[163] When asked in cross-examination about payment of the Symonds Street gain fee, Mr Millar admitted that there was a discussion between him and Mr Mephan about whether or not First NZ should pay the gain fee to ISL. He said:

> Mr Mephan raised with me and said you know in light of Barnes' fraud do you think we should pay ourselves this fee and I answered very clearly yes I did think we should pay ourselves this fee. The fraud was a matter that we were dealing with separately and would continue to do so.

## Causes of action pleaded by First NZ

[164] I note at the outset that there is an overlap in the amounts sought by First NZ as against different defendants and across various causes of action. As I will come to, there can be no double recovery.

### *Claims against ISL*

[165] First NZ alleges both breach of contract and negligence by ISL in making the payments referred to at [46] and [47] above. First NZ also claims in unjust enrichment against both ISL and Mr Millar. That is discussed at [304]–[313] below.

[166] My conclusion as to the nature of the ongoing arrangements between First NZ and ISL, after the sale of the Properties, is set out at [108] above. That is that the ongoing contract between First NZ and ISL required ISL to provide property management services from within the 3.25 per cent property management fee and did not provide for the payment of gain fees in respect of properties acquired after the last of the First NZ Properties was sold.

*Breach of contract*

[167] In relation to the breach of contract claim, First NZ says ISL:

(a) was not entitled to be paid for excess property management fees charged where no property management services were provided;

(b) was not entitled to appoint third parties Gravtec and Terra Firma to undertake the same property management services that ISL was already being paid to provide and to charge additionally for those services;

(c) was not entitled to direct the payments to Terra Firma and Gravtec;

(d) was not entitled to charge gain fees on the sale of future First NZ properties. In the case of both Kilmore Street and Symonds Street, there was no contractual basis to make payment of a gain fee. In the case of Kilmore Street, even if there were a contractual basis this was an insurance settlement and not a sale and therefore there was no basis for ISL to be paid a gain fee.

[168] First NZ says that in making the payments referred to in the preceding paragraph, ISL breached the terms of the new contract.

[169] In its second amended statement of claim First NZ claimed a total sum of $2,579,693.54 plus GST, being:

(a) $1,159,000.81 plus GST by way of disclosed property management fee;

(b) $183,220.00 plus GST, "excess" property management fees;

(c) $204,328.87 plus GST paid to Gravtec;

(d) $203,143.86 plus GST paid to Terra Firma;

(e) $380,000 plus GST for the Kilmore Street gain fee; and

(f) $450,000 plus GST for the Symonds Street gain fee.

Discussion

[170] As I have found, the continuing agreement between First NZ and ISL provided for a property management fee of 3.25 per cent of gross rentals. ISL continued to

receive payment of that amount (the disclosed management fee). As I have also found, cls 3.9 and 4.1 of the First NZ Management Agreement did not entitle ISL to claim for property management fees in addition to the 3.25 per cent. That was also the position after the Agreement came to an end in November 2004. The ongoing agreement between the parties did not therefore authorise ISL to pay itself the Opex management fee/"excess" property management fee. Nor was there a separate contractual basis for the payment.

[171] Mr Millar conceded there was no contractual basis for the $183,000 payment. It was in addition to the 3.25 per cent property management fee. It was not disclosed to shareholders and was effectively concealed because it was set off against the Opex received from tenants, so showed as neutral.

[172] In any event the defendants' evidence did not adequately establish their assertion that the "Opex management" was different from, and additional to, the property management function which ISL was already being paid to provide by way of the disclosed property management fee — that is the 3.25 per cent of gross rentals.

[173] Mr Mephan's evidence was that in practical terms Mr Eberlein of Gravtec carried out the property management function, including supervising Terra Firma. ISL itself undertook a very limited property management function, which Mr Mephan said included paying the Opex accounts, administering the banking and maintaining the accounting records. Mr Mephan described it as a "supervising, overarching function", carried out, at various times, by himself, Mr Barnes and Mr Millar. Mr Mephan acknowledged that ISL relied on Gravtec and Terra Firma as experts.

[174] In light of my earlier findings, nor was there a contractual basis as between First NZ and ISL for the engagement and payment of the third party providers, Gravtec and Terra Firma ($204,328.87 plus GST and $203,143.86 plus GST, respectively).

[175] However, there is no dispute that Gravtec and then Terra Firma actually carried out the property management services for which they were contracted.

[176] As to the gain fees, under the First NZ Management Agreement each property is defined as a "Property" and together they are defined in the Schedule to the Agreement as the "Properties". The Agreement contains no reference to the purchase of additional properties or to the payment of fees if additional properties were to be purchased.

[177] Clause 3 of the First NZ Management Agreement, as discussed at [150] above, also supports the view that the First NZ Management Agreement was focused on the acquisition and management of the Properties only.

[178] Clause 11.1(d) refers to a gain fee being payable on the sale of "any of the Properties". The last of the Properties was sold on 4 November 2004. Kilmore Street and Symonds Street were acquired subsequently. They did not fall within the definition of Properties and nor did the Agreement elsewhere refer to the payment of a gain fee on subsequently acquired properties.

[179] Even if the First NZ Management Agreement did continue in its existing form after the sale of the original Properties, it is in my view clear that the provision relating to payment of a gain fee must be interpreted as applying only to the original, defined Properties.

[180] There is no basis to imply a term or custom or practice allowing for the payment of a gain fee on other properties (and nor is this pleaded).

[181] There is no ambiguity. The plain meaning is that the gain fee is payable on the sale of the Properties.

[182] That being so, I accept that there was no entitlement to a gain fee for either of Kilmore Street or Symonds Street.

[183] Even if the First NZ Management Agreement, or the subsequent agreement, could be construed to provide for the payment of a gain fee on any subsequently acquired property, the Kilmore Street property was destroyed in an earthquake. There was no "sale" of the Kilmore Street property.

[184] The Kilmore Street gain fee was not disclosed with any annual accounts as a related party transaction. It was not included as part of the Management Fee reported in the 2013 Annual Accounts. In effect, the payment was disguised by the reporting of the proceeds of the disposal of the property as a net figure.

[185] First NZ is therefore entitled to payment of $830,000 in respect of the gain fees.

[186] I conclude that ISL was in breach of its contract with First NZ in authorising and/or making the payments referred to at [169] above and is entitled to recovery from ISL. While, as noted above, First NZ's second amended statement of claim sought a total amount of $2,579,693.54 plus GST, in closing submissions First NZ accepted that the amount claimed for disclosed management fees must take into account that it actually received property management services. First NZ's amended calculation of its loss is the disclosed property management fees of $1,159,000.81 plus GST, less the fees paid to Gravtec and Terra Firma, less a further amount of $77,500 plus GST paid to ISL. It is not clear what this last amount relates to.

[187] In a breach of contract claim, the plaintiff is to be put as nearly as possible into the position it would have occupied if the contract had been performed.[21] First NZ contracted ISL and paid it $1,159,000.81 plus GST for property management services. It received property management services. There was no contractual basis for the excess property management fees of $183,220.00 plus GST and I have found that no additional services were provided for that payment. There was no contractual basis (as between First NZ and ISL) for the fees paid to Gravtec and Terra Firma (totalling $407,472.73 plus GST). Nor was there a contractual basis for payment of the gain fees.

[188] Accordingly, in my view the appropriate way to calculate First NZ's contractual loss is the uncontracted for expenditure of $183,220 plus GST, plus $407,472.73 plus GST, plus the $830,000 plus GST gain fees.

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21 See for example *New Zealand Motor Bodies Ltd v Emslie* [1985] 2 NZLR 569 (HC) at 598.

*Negligence*

[189] First NZ alleges that ISL owed a duty of care to First NZ to perform administration and investment services with reasonable skill and care. The duty required ISL to take reasonable skill and care when making payments on First NZ's behalf: being fees for property management, payments to Gravtec and Terra Firma, and gain fees.

[190] First NZ claims that ISL negligently performed administration and investment services for First NZ, as agent for First NZ. It pleaded a consequential loss, or benefit to ISL, totalling $2,579,693.54 plus GST. The calculation of that amount is the same as for the breach of contract claim against ISL (set out at [169] above).

[191] ISL does not contend that these payments were not made and that ISL procured these payments to be made, but says the nature and extent of any duty of care it owed is set out in the First NZ Management Agreement. It is entitled to rely on that Agreement. ISL submits it did not owe First NZ a duty of care in tort — the relationship was not sufficiently proximate and there are wider policy considerations that tend to negative or restrict the existence of a duty in the circumstances of this case.[22]

[192] It also says that there is no evidence of what a reasonable investment manager would have done, for the purposes of comparison with what ISL actually did. Accordingly, there is no factual basis for a finding in negligence against ISL.

[193] ISL also relies on the indemnity and limitation of liability provisions in cls 6 and 7 of the First NZ Management Agreement and I consider that question in relation to the affirmative defences discussed later in the judgment.

<u>Discussion</u>

[194] Justice Glazebrook set out the test for ascertaining whether a duty of care exists in *Rolls-Royce New Zealand Ltd v Carter Holt Harvey Ltd* as follows:

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22 *Rolls-Royce New Zealand Ltd v Carter Holt Harvey Ltd* [2005] 1 NZLR 324 (CA) at [58].

> [58] … The ultimate question when deciding whether a duty of care should be recognised in New Zealand is whether, in light of all the circumstances of the case, it is just and reasonable that such a duty be imposed. The focus is on two broad fields of inquiry but these provide only a framework rather than a straitjacket. The first area of inquiry is as to the degree of proximity or relationship between the parties. The second is whether there are other wider policy considerations that tend to negative or restrict or strengthen the existence of a duty in the particular class of case. At this second stage, the Court's inquiry is concerned with the effect of the recognition of a duty on other legal duties and, more generally, on society.

[195] I accept that ISL was sufficiently proximate. The parties were in a contractual relationship, this being the undocumented arrangement that continued after the sale of the last of the First NZ Properties. Under this contract, ISL had an obligation to provide administration and investment services to First NZ. As First NZ notes by way of illustration of that relationship, ISL had "complete control" over the property companies, including their banking arrangements.

[196] I also accept that the fact of common directors of First NZ and ISL (Mr Millar and latterly Mr Mephan), and the merged meetings of ISL and the property companies, meant that knowledge within one entity can be imputed to the other.

[197] It was therefore reasonably foreseeable that if ISL did not exercise reasonable skill and care in performing its contractual obligations, harm would be caused to First NZ.

[198] There are no policy reasons that preclude the imposition of a duty of care on ISL in this situation. A duty on an investment manager is commonplace where there is a contractual relationship between the parties.[23] The tortious duty is concurrent and coextensive with the contractual relationship between the parties.

[199] While generally contractual and tortious duties should be coextensive, a broader duty in tort may be found in some circumstances. Here, First NZ says that the duty of care in tort is wider than the contractual duty in the circumstances of a conflict of interest. As Tipping J said in *Frost & Sutcliffe v Tuiara*,[24] in the context of a contractual relationship between a law firm and its clients, "in some circumstances it

[23] *Frost & Sutcliffe v Tuiara* [2004] 1 NZLR 782 (CA) at [17].
[24] At [19]–[22].

may be necessary, for example to avoid professional impropriety, to hold that the duty in tort is wider than that in contract”.[25]

[200] I accept that the circumstances of this case come within the exception to Tipping J’s general rule. Even if the First NZ Management Agreement continued beyond 2004 (which I have concluded it did not) it would be appropriate to impose a duty of care on ISL in tort, notwithstanding the purported limitations contained in cl 6 of the Agreement.

[201] The duty of care owed by ISL was to exercise a reasonable standard of care in performing its management obligations to First NZ. I accept that this required ISL to ensure that there was a proper basis for charging First NZ, or allowing it to be charged, property management fees and other fees; and the fees that were actually charged by ISL to carry out its management obligations were not excessive.

[202] I also conclude that ISL did not at any stage undertake such an assessment. Throughout it relied on its (effectively Mr Millar’s) own interpretation of the written First NZ Management Agreement, and that Agreement continuing past November 2004, despite the “Properties” to which it applied having all been sold.

[203] ISL has maintained that at all times it was entitled to a 6.50 per cent management fee. The experts for all parties accept that ISL was paid over and above this 6.50 per cent fee, including:

(a) the Excess Property Management fees, totalling $183,220 plus GST;

(b) the property management fees paid to Gravtec, totalling $204,328.87 plus GST; and

(c) the property management fees paid to Terra Firma, totalling $203,143.86 plus GST.

[204] As noted, ISL had complete control over First NZ’s banking arrangements.

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25 At [20].

[205] I conclude that, in making the undisclosed payments to Gravtec and the undisclosed payments to Terra Firma, in addition to the 3.25 per cent disclosed property management fee, ISL breached its duty of care to First NZ.

[206] ISL was also in breach of its duty of care to First NZ in authorising and making the payment to itself of the excess property management fees, where there was no written or other agreement with First NZ to charge property management fees over and above the agreed management fee.

[207] ISL was also in breach of its duty of care to First NZ in authorising and making payment of the gain fee of $430,000 plus GST on the insurance settlement of the Kilmore Street property, which was not a sale (noting that the amount claimed is $380,000 plus GST), and a gain fee of $450,000 plus GST on the sale of the Symonds Street property. As I have already concluded, there was no contractual basis for the payment of these fees and no evidence that ISL sought to ascertain a proper basis for the payments. To the contrary, Mr Mephan's exchange with Mr Millar on whether the Symonds Street gain fee should be paid (referred to at [163] above) could be seen as a deliberate decision by Mr Millar not to inquire further as to a proper basis for that payment.

[208] I do not accept ISL's submission that there is no causal link between its negligent conduct and any loss suffered by First NZ.

[209] The causal link in respect of the gain fees is unarguable. That loss totals $830,000 plus GST.

[210] In respect of all aspects of the loss claimed — the excess property management fees, the payments to Gravtec and Terra Firma and the gain fees — ISL was in effect the sole actor. It occasioned the payment of those amounts by First NZ without inquiry as to a proper basis for doing so.

[211] First NZ is entitled to be put in the position it would have been in had ISL's negligence not occurred.

[212] I apply the same calculation as in relation to the breach of contract claim, set out at [188] above. ISL is liable to pay First NZ the uncontracted for expenditure of $183,220 plus GST, plus $407,472.73 plus GST, plus the $830,000 plus GST gain fees.

***Claims against Mr Millar and Mr Mephan***

[213] The plaintiffs say Mr Millar and Mr Mephan[26] were fiduciaries of the property companies and owed fiduciary duties to those companies which required them:

(a) To act in good faith.[27]

(b) Not to profit from the property companies.[28]

(c) Not to place themselves in a position where duty and interest may conflict.[29]

(d) Not to act for their own benefit or for the benefit of a third person without the informed consent of their principal.[30]

[214] First NZ alleges that, at all material times, Mr Millar and Mr Mephan failed to fulfil their fiduciary duties to the company.

[215] First NZ also alleges breach by both Mr Millar and Mr Mephan of s 131 of the Companies Act, which restates the basic common law duty of directors to the company, and s 137 of the Companies Act, which requires a director to exercise the care, skill and diligence of a reasonable director, when exercising powers or performing duties.

[216] The plaintiffs plead that Mr Millar's personal interests conflicted with his duties to First NZ and the other property companies. He was a director of each of the property companies, a director of ISL and with effective power to appoint directors to

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26 Only in respect of First NZ and Springs Road.
27 *Holden v Architectural Finishes Ltd* HC Wellington M659/92, 1 November 1995 at 84: "… to act as the director honestly sees as being in the best interests of the company."
28 *Holden v Architectural Finishes Ltd*, above n 27.
29 *Stevens v Premium Real Estate Ltd* [2009] NZSC 15, [2009] 2 NZLR 384 at [71].
30 At [72].

the property companies. Mr Millar used his power to appoint and remove directors to the property companies to install other directors whose loyalty was to him first, rather than to the company. At various times, Mr Millar appointed his wife, his son-in-law, his employees and his contracted staff. He held "merged" meetings of the property companies and ISL.

[217] This was in breach of his duties of loyalty and good faith, and to act in the best interests of the property companies.

[218] Mr Millar profited from the arrangements, in breach of his duty not to profit from his position.

[219] The plaintiffs say that Mr Mephan was in a similar position to Mr Millar, although for a more limited period.

[220] From 13 February 2018 to 21 April 2020 Mr Mephan was a director of all three property companies. He received no director's fees from those companies.

[221] From February 2018 to April 2020, Mr Mephan was CEO of ISL, providing services through his company Corvus Consulting. Mr Mephan was not a director of ISL.

[222] Mr Mephan is Mr Millar's son-in-law. His partner (Mr Millar's daughter) was a beneficiary of the Kaiuma Family Trust, the sole shareholder of ISL.

[223] That meant, First NZ says, that Mr Mephan was in a position where his personal interests conflicted with his duties to First NZ. In authorising the payments discussed above he also was in breach of his duties of loyalty and good faith and to act in the best interests of First NZ. He profited from his position.

[224] Among the breaches of duty pleaded by First NZ against both Mr Millar and Mr Mephan is that they failed to identify or take reasonably practicable steps to prevent the fraud by Mr Barnes.

[225] Mr Barnes was employed by ISL as a financial manager on 7 May 2001. He was appointed as director of First NZ on about 25 June 2001. Under an agreement dated 21 November 2017, but deemed to commence on or about 1 April 2007, ISL appointed Mr Barnes, through his company Activa to perform the role of CEO for ISL. That agreement was signed by Mr Millar on behalf of First NZ. As CEO of ISL, Mr Barnes had complete control of First NZ's financial operations.

[226] Mr Barnes committed fraud against First NZ over an approximate 10-year period. To date, approximately $966,000 has been recovered from Mr Barnes.

[227] The plaintiffs say that, while it was open for Mr Millar and Mr Mephan to seek the informed consent of their principals to the conflicts discussed above, they did not do so, in that they did not make adequate disclosure of their interests.

[228] Mr Stobo's expert evidence for the plaintiffs was that the property companies' annual reports should have provided for the full disclosure of the interests of all of ISL, Gravtec, Neil Barnes and Activa Consulting, but did not do so.

[229] Mr Millar did not accept that the potential conflict of interest had any negative consequences for the property companies. In relation to his s 131 duties, Mr Millar said that he had a genuinely held subjective belief, reasonable in the circumstances, that he was acting in the best interests of the companies.[31]

[230] The first and third defendants submitted that the claim of negligence under s 137 of the Companies Act must fail because, first, the plaintiffs did not bring evidence of what a reasonable director ought to have done, by comparison with what actually occurred. Second, the remedy under s 137 is loss-based and there was no evidence of any loss.

[231] The essence of the submissions advanced for Mr Mephan was that the deficiencies in practice identified by the plaintiffs may indicate that best practice was not followed, but Mr Mephan did not act unlawfully or carelessly or in breach of his fiduciary duties.

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[31] *Madsen-Ries (in liq) v Cooper* [2020] NZSC 100, [2021] 1 NZLR 43 at [112].

*Requirements of a fiduciary*

[232] The relationship of the director and company is an established category of relationship which is inherently fiduciary.[32]

[233] In *Bristol and West Building Society v Mothew*, Millet LJ summarised the requirements of a fiduciary:[33]

> The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or for the benefit of a third person without the informed consent of his principal.

[234] The key fiduciary duties applicable to directors are:

(a) Directors should not enter into transactions where their interests conflict or might conflict with those of the company, without obtaining appropriate consent; and

(b) Directors should not benefit in any way from their office, without appropriate approval of their doing so.

[235] A director is accountable for profit arising by reason of and in the course of his or her fiduciary office.[34]

*Statutory provisions*

[236] The duties under s 131 are essentially the same duties as the fiduciary duties of good faith and loyalty.[35] Section 131 provides:

> **131 Duty of directors to act in good faith and in best interests of company**
>
> (1) Subject to this section, a director of a company, when exercising powers or performing duties, must act in good faith and in what the director believes to be the best interests of the company.

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32 *Ng v Harkness Law Ltd (No 2)* [2014] NZHC 1667 at [7]; and *New Zealand Netherlands Society "Oranje" Inc v Kuys* [1973] 2 NZLR 163, [1973] 2 All ER 1222 (PC) at 166.

33 *Bristol and West Building Society v Mothew* [1988] Ch 1, [1996] 4 All ER 698 at 18, cited in *Stevens v Premium Real Estate*, above n 29, at [67].

34 *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134, [1942] 1 All ER 378 (HL) at 147–149.

35 *Torbay Holdings Ltd v Napier* [2015] NZHC 2477, [2015] NZAR 1839 at [153].

> (2) A director of a company that is a wholly-owned subsidiary may, when exercising powers or performing duties as a director, if expressly permitted to do so by the constitution of the company, act in a manner which he or she believes is in the best interests of that company's holding company even though it may not be in the best interests of the company.
>
> (3) A director of a company that is a subsidiary (but not a wholly-owned subsidiary) may, when exercising powers or performing duties as a director, if expressly permitted to do so by the constitution of the company and with the prior agreement of the shareholders (other than its holding company), act in a manner which he or she believes is in the best interests of that company's holding company even though it may not be in the best interests of the company.
>
> (4) A director of a company that is carrying out a joint venture between the shareholders may, when exercising powers or performing duties as a director in connection with the carrying out of the joint venture, if expressly permitted to do so by the constitution of the company, act in a manner which he or she believes is in the best interests of a shareholder or shareholders, even though it may not be in the best interests of the company.

[237] Section 137 provides:

> **137 Director's duty of care**
>
> A director of a company, when exercising powers or performing duties as a director, must exercise the care, diligence, and skill that a reasonable director would exercise in the same circumstances taking into account, but without limitation,—
>
> (a) the nature of the company; and
>
> (b) the nature of the decision; and
>
> (c) the position of the director and the nature of the responsibilities undertaken by him or her.

*Mr Millar*

[238] Mr Millar acknowledged that he owed fiduciary duties and duties under s 131 of the Companies Act to the plaintiff companies.

[239] Applying the test in *Bristol and West Building Society v Mothew*,[36] First NZ did not have Mr Millar's single-minded loyalty. Throughout the relevant period he was in a position where his personal interests conflicted with his duties to the property companies. Those conflicting interests were:

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36 *Bristol and West Building Society v Mothew*, above n 33, at 18, cited in *Stevens v Premium Real Estate*, above n 29, at [67].

(a) He was a director of each of the property companies.

(b) He was a director of ISL, service provider to the property companies.

(c) ISL retained the right to appoint and remove directors of the property companies from 2001 onwards. Mr Millar accepted that, in practice, the effect of ISL retaining that power for the duration of his directorship was the same as him having the power of appointment himself. He exercised that power, appointing:

   (i) his wife, Gillian Bishop;

   (ii) his son-in-law, Mr Mephan;

   (iii) ISL's former CEO, Neil Barnes;

   (iv) his former ISL employee, Virginia Laughton; and

   (v) ISL's former CEO and property manager, Mr Penrose.

(d) ISL was owned by the Kaiuma Family Trust. Mr Millar's children are the beneficiaries of the Trust. He derived his income from ISL.

[240] Mr Millar was in a situation of irreconcilable conflict of interest — it was favourable for ISL to continue to provide services to First NZ, regardless of whether that was in the best interests of First NZ.

[241] I accept First NZ's submission that the termination of the First NZ Franklin Agreement provided an opportunity for ISL to increase the amount it received from First NZ. ISL went from a situation where it charged First NZ, and continued to receive from First NZ, 6.50 per cent of rentals, from which it paid Franklin to provide property management services, to providing the services in-house, more cheaply than the cost of engaging Franklin. As at [112] above, the cost to engage Mr Penrose was a fraction of the cost of engaging Franklin. ISL then went to a situation where it received 6.50 per cent of the rentals, plus $183,000 for "opex management", while

property management services were actually provided by Gravtec and Terra Firma (paid for by Opex).

[242] Further the Sheffield Crescent and Kilmore Street properties had significantly higher rentals than the original First NZ Properties and therefore a significantly higher management fee for ISL — the fee effectively doubled. That was accepted by Ms Kelly, expert witness for the defendants.

[243] Mr Millar used his effective power of appointment of directors of First NZ to appoint directors he knew would be loyal to him personally (as at [216] above). He terminated Mr Mephan's directorship when Mr Mephan obtained legal advice that said potentially there was legal action available against Mr Millar.

[244] ISL and PPML entered into a heads of agreement on 1 May 2020 under which ISL was to assign its Management Agreements with each of the three property companies to PPML for consideration of $345,000. Mr Millar signed the heads of agreement for ISL. About one week after the heads of agreement, Mr Millar appointed Mr Penrose as a director of each of the plaintiff companies.

[245] The heads of agreement included a clause that said in relevant part:

> In order to protect and maintain ISL's professional indemnity insurance coverage, PPML agrees that neither it nor any of its agents, officers or employees will take any steps, directly or indirectly, to support, bring or provide information necessary to support or bring any claim against ISL or its directors and officers unless required by law.

[246] There were no independent directors of First NZ (or the other property companies), either at the time of the termination of the Franklin agreement (31 December 2003) or at the date of the sale of the last of the First NZ Properties (4 November 2004). The other two directors of First NZ at both those points were Mr Millar's employees, Ms Laughton and Mr Barnes. Mr Millar accepted that in fact there was no independent director of the property companies from February 1998 when Sir Allan Wright ceased to be a director.

[247] That situation of conflict was compounded by Mr Millar effectively treating all the property companies and ISL as one entity, with meetings combined for all three

of the property companies and ISL. Mr Millar acknowledged that the meetings were conducted as one meeting; while agreeing they were separate enterprises, in his view not to the extent they required separate meetings. Mr Millar was also the person with overall control of the property companies' books and banking arrangements.

[248] It was open to Mr Millar to seek First NZ's informed consent to him continuing to act with a potential conflict of interest. In *Stevens v Premium Real Estate*, the Supreme Court said:[37]

> Of course a duty of this kind can be modified by an informed agreement or consent on the part of the principal. … Whether a disclosure has been sufficient in the circumstances must depend upon the facts of each case. The requirement is for the principal's informed consent to the agents acting with a potential conflict of interest. An informed consent is one which is given in the knowledge that there is a conflict of interest between the parties. The burden of proof of adequate disclosure is on the agent. The vendor/principal would need to have been told enough to appreciate that a real conflict of some kind existed for the agent.
>
> (footnote omitted)

[249] Mr Millar did not seek consent of any of the property companies to continuing to act, notwithstanding his conflict. There was no evidence that, at relevant times, Mr Millar took any steps to attempt to manage the conflict.

[250] Mr Millar relies on the fact that the relationship between ISL and the property companies was clear at all times and that he disclosed that he was a director of ISL. However, Mr Stobo's expert evidence for the plaintiffs was that the property companies' annual reports should have provided for the full disclosure of the interests of all of ISL, Gravtec, Neil Barnes and Activa, but did not do so. Nor was there specific disclosure of the nature of the changed property management arrangements at any time. General disclosure under s 140 of the Companies Act does not override a director's s 131(1) duty. A director cannot, by disclosing his personal or other interests or conflicts, avoid liability under s 131 if he or she fails faithfully to consider, and act in, what is in the company's best interests.[38] Similarly, in relation to a director's fiduciary duties.

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[37] *Stevens v Premium Real Estate*, above n 29, at [72].
[38] *Hedley v Albany Power Centre Ltd (in liq) (No 2)* [2006] 2 NZCCLR 1148 (HC) at [16].

[251] For example, the only disclosure of the change from Franklin to an in-house property manager was in the 2004 Annual Report for Foodstore Properties Ltd, where Mr Millar (and at that time also Mr Barnes) reported:

> Property Management
>
> Until 1 January 2004, the Manager had utilised the services of The Franklin Company with regard to property management. The Manager terminated the agreement with The Franklin Company from that date and now all property management is dealt with by the Manager's in-house property manager. There has been no change in the total management fees paid by the company.

[252] There was no review at the point when ISL terminated the agreement with Franklin as to how First NZ's Properties were to be managed and whether the funding of that management should change — specifically whether it was in the best interests of First NZ to continue to charge that amount. The effect of continuing to do so was that ISL was immediately able to increase its earnings from the Management Agreement.

[253] Although the in-house property manager was substantially cheaper than Franklin, that was not disclosed. See, for example, a comparison of the costs at [112] above.

[254] In the absence of any specific discussion and agreement about the terms of the ongoing arrangement, and given Mr Millar's clear conflict of interest, he was obliged to specifically raise with First NZ any change to the previous arrangement, whereby half of the 6.50 per cent management fee was applied to property management. There is no evidence that he did so.

[255] Nor did Mr Millar disclose to First NZ the payment of the $183,000 excess property management fee charged by ISL in addition to the Property Management Fee.

[256] In addition, the properties purchased after the sale of the last of the First NZ Properties, Sheffield Crescent and Kilmore Street, had significantly higher rentals, with the consequence that the management fee to ISL increased accordingly. Effectively the rent, and the management fee, doubled.

[257] Mr Millar did not accept that his position of conflict of interest had any negative consequences for the property companies. I agree with the plaintiffs' assessment that Mr Millar's defence to the claims against him can be characterised as a sense of entitlement, with little, if any, recognition of his obligations to the plaintiff companies.

[258] As to the gain fees, I conclude that Mr Millar did breach his fiduciary duties owed to First NZ by directing the payment of the Kilmore Street gain fee, in circumstances where there was no proper contractual basis to make the payment and it was not in the best interests of First NZ. By directing the payment of the gain fees, Mr Millar indirectly profited at the expense of First NZ, Mr Millar also failed to exercise due care and skill to establish an obligation on the part of First NZ to make the payments.

[259] I accept First NZ's submission that there was no apparent consideration by Mr Millar of what was in the best interests of First NZ in relation to the gain fees. Mr Mephan on the other hand did appear to have some hesitation over authorising the Symonds Street payment.[39]

[260] Overall, I find that Mr Millar was in a position where his own interests conflicted with the interests of his principal, First NZ; he did not make adequate disclosure of that conflict nor seek informed consent to nevertheless continuing.

[261] Mr Millar profited from the arrangements, in breach of his duty not to profit from his position as a director of the plaintiff companies. While Mr Millar was not paid as a director of the property companies, in relation to ISL, the shares in ISL were held by the Kaiuma Family Trust. Mr Millar's children are beneficiaries of the Trust. Mr Millar earned his income, or a large portion of it, from ISL. ISL accounts record his salary and also "shareholders' drawings" which Mr Millar acknowledged may have been payments to him. ISL received profits from the payments made to it by the property companies. As Mr Millar acknowledged, the better ISL did, the better he did.

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[39] See [163] above and [287] below.

Section 131

[262] As noted above, the submission for Mr Millar in relation to s 131 of the Companies Act was that it was enough that he had a genuinely held subjective belief, reasonable in the circumstances, that he was acting in the best interests of the property companies.[40]

[263] However, as the Supreme Court said in *Madsen-Ries*, although the s 131 test is subjective:[41]

> … directors will probably have a hard task persuading the court that they honestly believed that an act or omission that resulted in substantial and foreseeable detriment to the company was in the company's best interests. Under a subjective test, the fact that an allegedly unreasonable belief was held may, however, provide evidence that the belief was not honestly held.
>
> (footnotes omitted)

[264] The Court's judgment also referred to a number of exceptions and qualifications to the subjective test,[42] including where there is no evidence of actual consideration of the best interests of the company, where there is a conflict of interest or where the action was one that no director with any understanding of fiduciary duties could have taken.

[265] Other authorities are to similar effect. As Fogarty J put it in *Sojourner v Robb*:[43]

> In this context, the standard in s 131 is an amalgam of objective standards as to how people of business might be expected to act, coupled with a subjective criterion as to whether the directors have done what they honestly believe to be right. The standard does not allow a director to discharge the duty by acting with a belief that what he is doing is in the best interest of the company, if that belief rests on a wholly inappropriate appreciation as to the interests of the company.

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[40] *Madsen-Ries (in liq) v Cooper* [2020] NZSC 100, [2021] 1 NZLR 43 at [112].

[41] At [109]. This passage was cited by the High Court in *Probitas Systems Ltd (in liq) v Clark* [2022] NZHC 1219 at [25] where the Court concluded that the director was in breach of s 131.

[42] At [113] (footnotes and citations omitted).

[43] *Sojourner v Robb* [2006] 3 NZLR 808 (HC) at [102], cited in *Vercauteren v B-Guided Media Ltd* [2011] NZCCLR 9 (HC) at [52].

[266] Where a director acts in a way that no director with any understanding of fiduciary duties would act, that director's belief that an action was in the best interest of the company will not prevent a finding of a breach of duty.[44]

[267] As I have found, Mr Millar had a conflict of interest between his own and ISL's interests on the one hand, and the property companies' interests on the other, throughout the period in question. As already noted, there was no evidence that Mr Millar actually considered the best interests of the plaintiff companies, beyond the bare fact of ensuring that the plaintiffs' obligations to provide property management services to their tenants were met. Mr Millar could not reasonably have believed that the ongoing arrangements were in First NZ's best interests.

[268] I find that the exception in *Madsen-Ries* is engaged. Mr Millar was in breach of the duties he owed to First NZ under s 131.

Section 137

[269] Section 137 of the Companies Act requires a director to exercise the care, skill and diligence of a reasonable director, when exercising powers or performing duties.

[270] The relevant standard is an objective one: a "reasonable director".[45] The director's position and responsibilities may be taken into account, but the director's knowledge and experience is not relevant. The High Court said in *Richard Geewiz Gee Consultants Ltd (in liq) v Gee*:[46]

> Section 137 is the statutory expression of the directors' duty of care and skill. The standard to be applied is that of the reasonably competent director. The director's personal knowledge and experience is no longer relevant. At the same time, however the reference in paragraph (c) to the position of the director and the nature of the responsibilities undertaken by him or her introduces an element of subjectivity.

[271] Both Mr Millar and Mr Mephan were required to exercise their powers, and perform their duties as directors, to this standard. The plaintiffs say they breached the

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44 *Vercauteren v B-Guided Media Ltd*, above n 43, at [52], citing *Shuttleworth v Cox Bros & Co (Maidenhead) Ltd* [1927] 2 KB 9 at 18 per Banks LJ.

45 *Morgenstern v Jeffreys* [2014] NZCA 449, (2014) 11 NZCLC 98-024 at [89].

46 *Richard Geewiz Gee Consultants Ltd (in liq) v Gee* [2014] NZHC 1483 at [105] (footnote omitted).

s 137 duty by acting as directors of the property companies while also being a director or CEO, respectively, of ISL and having a beneficial interest in ISL; authorising the payments from the property companies to ISL and to Terra Firma and Gravtec; in respect of First NZ, authorising the payment of the gain fees to ISL.

[272] Mr Stobo, in his evidence for the plaintiffs, applied the standard required of a reasonable director and said that reasonably practical steps Mr Millar and Mr Mephan ought to have taken would include:

(a) providing shareholders in their Annual Reports with a rationale for the selection of Franklin, Activa, Terra Firma and Gravtec;

(b) periodic reviews of the management performance of those companies;

(c) periodic reviews of fee structures and value for those fees given changing market conditions.

[273] The first defendant's response was that the plaintiffs did not provide evidence of what a reasonable director ought to have done. In any event, the remedy under s 137 is loss-based and there was no evidence of loss caused by any of the conduct on which the negligence claims were based.

[274] I conclude that Mr Millar was in breach of his obligations under s 137. He was a director of the plaintiff companies and of ISL from the outset. He was intimately familiar with the operations of the companies.

[275] He failed to adequately disclose his position of conflict at any relevant point, as would be expected of a reasonable director. He took no steps to explain or review the nature of and payment for the property management services to First NZ at the point of, for example, termination of the Franklin agreement, or the engagement of each of Gravtec and Terra Firma. As I have found, Mr Millar did not ensure that full disclosure of the effect of the changed arrangements was made. He did not take steps to ensure there was a proper basis for the payment of the gain fees.

[276] I do not accept the defendants' submission that First NZ needed to have called specific evidence as to what would have been required of a reasonable director. It seems to me that requirements of the kind outlined above (at [272]) were self-evident.

[277] Monetary compensation may be awarded for breach of fiduciary duty.[47] The aim is to restore the plaintiff to the position it would have been in but for the breach.

[278] In this case I am satisfied that First NZ may recover against Mr Millar excess property management fees of $183,220 plus GST, the fees paid to Gravtec of $204,328.87 plus GST, the fees paid to Terra Firma of $203,143.86 plus GST, and the gain fees of $830,000 plus GST.

*Mr Mephan*

[279] The plaintiffs say that Mr Mephan was in a similar position to Mr Millar in light of the factors set out at [220]–[222] above that rendered him a fiduciary in a position of conflict.

[280] But Mr Mephan's circumstances are somewhat different from those of Mr Millar. He was not a director of ISL. Unlike Mr Millar, Mr Mephan did not have effective power of appointment of the plaintiff companies' directors.

[281] The other potentially significant difference between Mr Mephan and Mr Millar is that the former was involved with ISL and the plaintiff companies relatively late in the piece, and had no role with them during the period of the Franklin Agreements. It cannot be assumed that he knew about the arrangements whereby half of the management fee paid by First NZ to ISL was applied to the property management services provided by Franklin. Nor was he involved when the last of the First NZ Properties were sold in November 2004. Against that, though, Mr Mephan acknowledged in cross-examination that he did not ask to see the relevant Management Agreements when he was appointed. However, Mr Mephan did go about

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[47] *Day v Mead* [1987] 2 NZLR 443 (CA); and *Aquaculture Corp v New Zealand Green Mussel Co Ltd* [1990] 3 NZLR 299 (CA). See also *Chirnside v Fay* [2006] NZSC 68, [2007] 1 NZLR 433 and *Premium Real Estate v Stevens*, above n 29, where the Supreme Court accepted as a given that monetary compensation might be awarded for breach of fiduciary duty.

getting independent accounts and it was through this process that the Barnes fraud was detected. He also sought legal advice referred to below. It was in those circumstances that Mr Millar required him to resign from his role at ISL and as a director of the property companies.

[282] While Mr Mephan refuted the suggestion that he resigned because of differences with Mr Millar, several factors give rise to an inference that Mr Mephan was at the least uncomfortable with the way the relationship was being conducted. First, his query about payment of the gain fee on the sale of Symonds Street, referred to at [163] above. Second, the circumstances of his resignation. Mr Millar wrote to Mr Mephan on 9 April 2020. In that letter he said:

> *It is apparent to me, from the recent correspondence and discussions that we have had, that you and I have different views on how issues involving Neil Barnes' defalcations should be handled on an on-going basis. My view is that we should continue to work through the process of recovery from Barnes ... and then, if there is a shortfall, seek advice on liability if any for such shortfall. As I understand it, you are wanting to move straight to the point of seeking recovery from ISL and myself.*
>
> ...
>
> *I am prepared to take control of these issues and to assume the associated risks.*
>
> *In these circumstances, it seems our professional relationships should be brought to an end. Those relationships are:*
>
> > *(i) The CEO positions you have with ISL and the property companies.*
> >
> > *(ii) The directorships you hold on those same companies.*
>
> (emphasis in original)

[283] In cross-examination, Mr Mephan clarified that, at the time of Mr Millar's letter, he had advice to say that potentially there was action that could be taken against Mr Millar, rather than that he was looking to Mr Millar and ISL for recovery.

[284] While Mr Mephan without doubt owed fiduciary and s 131 duties to the plaintiff companies and was in a position of potential conflict, given he was a director of the property companies and his income derived from ISL, Mr Mephan lacked the knowledge necessary to understand that the property management arrangements

entered into — in-house, Gravtec and Terra Firma — were not in the plaintiff companies' best interests, having regard to what I have found was the longstanding nature of the agreements between those parties. Also relevant was that Mr Millar had control of the banking arrangements for the property companies.

[285] For those reasons, I accept that, in terms of s 131 of the Companies Act, Mr Mephan may have had a genuinely held and reasonable belief that he was acting in the best interests of First NZ (and the other property companies) in entering into the various property management arrangements. Taking all of these factors into account, I conclude that in relation to the claims against him in relation to the property management fee, the excess property management fees and the payments to Gravtec and Terra Firma, Mr Mephan did not act in breach of his fiduciary or s 131 duties.

[286] As to s 137, while that provision imposes an objective standard ("reasonable director"), the requirement to have regard to the position of the particular director and the nature of the responsibilities undertaken, introduces an element of subjectivity. That requires the Court to have regard to Mr Mephan's role within the company structure and in a particular time and context. While in hindsight Mr Mephan might have done more, it is relevant that he was appointed as a director some 14 years after termination of the Franklin management agreements, where Mr Millar had effective control of both ISL and the property companies (including the property companies' banking arrangements), Mr Millar was his father-in-law and, I infer, expected obedience and compliance from Mr Mephan.[48] Notwithstanding that, as I have noted already, it was Mr Mephan's inquiries that led to Mr Barnes' fraud being exposed and Mr Mephan who sought legal advice as to possible next steps. I do not think his behaviour can be characterised as negligent.

[287] I do not think the same can be said of the Symonds Street gain fee. As already discussed, Mr Mephan had expressed to Mr Millar some doubt about the appropriateness of the payment. Even assuming that Mr Mephan was unaware of the history of the First NZ Management Agreement, in light of that concern he ought to have ascertained a clear contractual basis for payment of the fee before authorising it.

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[48] See by analogy *Grant v Johnston* [2016] NZCA 157.

Even on the assumption that Mr Mephan was aware of the terms of the First NZ Management Agreement and thought it remained in place on its terms, as already discussed, the Agreement referred to the payment of a gain fee only in respect of the original, defined, "Properties". Symonds Street was not one of them. Mr Mephan ought, at the least, to have sought legal advice as to whether the Agreement could legitimately be construed to encompass subsequently acquired properties.

[288] I conclude that Mr Mephan was in breach of his duties to First NZ in authorising the payment of the Symonds Street gain fee to ISL. Despite being on "alert", he did not ascertain a clear and proper basis for claiming a gain fee on the sale of the Symonds Street property. I conclude that he was in breach of Mr Mephan's fiduciary duties and his obligations under ss 131 and 137 of the Companies Act.

[289] First NZ is entitled to recover from Mr Mephan $450,000, being the Symonds Street gain fee.

*Claim in relation to Barnes' fraud*

[290] Despite the pleading that Mr Millar and Mr Mephan failed to identify or take reasonably practicable steps to prevent the fraud by Mr Barnes, that aspect of the claim was not pursued with any vigour at trial. In any event, as the defendants submit, it is not relevant to the recovery sought or causative of any of the alleged losses. The amounts that are the subject of the Barnes fraud were the subject of a full and final settlement between the parties. Given that, I do not discuss the Barnes question further in this judgment.

***Knowing receipt***

[291] First NZ claims in knowing receipt against Mr Millar in relation to the property management fee ($1,159,000.81 plus GST), the excess property management fees ($183,220.00 plus GST) and the gain fees ($380,000 plus GST and $450,000 plus GST).

[292] A company may have a personal claim for knowing receipt in respect of a director's breach of their fiduciary duty,[49] when the third party received property that is tainted by their knowledge that the transfer of that property involved a breach of fiduciary duties owed by a director to a company. Liability arises when it is unconscionable for the recipient to retain property because of the recipient's state of knowledge.[50]

[293] The elements necessary to establish a knowing receipt claim are:[51]

(a) disposal of assets the subject matter of fiduciary obligations owed to the plaintiff;

(b) the beneficial receipt of assets subject to fiduciary obligations; and

(c) knowledge on the part of the defendant that the assets received were subject to a breach of fiduciary duty.

[294] First NZ says Mr Millar received the assets listed at [291] above with knowledge that ISL had no lawful entitlement to the payments. First NZ submits that the law is not yet settled about what constitutes knowledge on the part of the defendant.[52] The Court of Appeal held in *McLennan v Livaja* that actual knowledge and wilful blindness are sufficient,[53] but First NZ suggests that lesser states of mind may also suffice.

[295] In any event, in First NZ's submission Mr Millar had actual knowledge of the transfer of the funds because he approved the transactions that transferred the sums of money when he was the director of ISL and of the property companies. Nor can there be any doubt that ISL received the assets.

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49 Lynne Taylor and Matthew Berkahn "Remedies for Breach of Fiduciary Duty" in *Company Law – A to Z of New Zealand law* (online ed, Westlaw) at [16.28.2].

50 *Bank of Credit and Commerce (Overseas) Ltd v Akindele* [2001] Ch 437 (CA) at 455, cited in *McLennan v Livaja* [2017] NZCA 446, [2018] NZAR 405 at [38].

51 *Torbay Holdings Ltd v Napier*, above n 35, at [184], citing *El Ajou v Dollar Land Holdings* [1994] 2 All ER 685 (CA) at 700; *Equiticorp Industries Group Ltd (in stat man) v R* [1998] 2 NZLR 481 (HC); and *Scott v ANZ Bank New Zealand Ltd* [2020] NZHC 906, [2020] 3 NZLR 145 at [101].

52 *Scott v ANZ Bank New Zealand Ltd*, above n 51, at [109]–[138].

53 *McLennan v Livaja*, above n 50.

[296] First NZ says liability is personal, and the purpose of the liability is to restore the property lost by the unconscionable receipt to the beneficiaries.[54]

[297] Mr Millar says he did not actually receive the amounts in question and therefore the knowing receipt claim against him must fail.

*Discussion*

[298] In *McLennan v Livaja* the Court of Appeal clarified the law of knowing receipt:[55]

> A claim for knowing receipt, however, depends on the tainted circumstances of receipt of property. Liability will arise where it is unconscionable for the recipient to retain it because of the recipient's state of knowledge in respect of the fact that the transfer involved a breach of fiduciary obligations owed by the transferor.
>
> Different High Court judgments have described the basis for knowing receipt as either unconscionability or unjust enrichment, a divergence possibly arising from the nature of the remedy applied in such cases. This in turn has led to differing conclusions as to the level of knowledge required to establish liability.
>
> We consider that the correct basis for knowing receipt is unconscionability. We prefer to characterise the liability incurred on a finding of knowing receipt as a personal liability to account in equity to the beneficiaries by restoring the property lost by the unconscionable receipt. The core duty of that liability is to restore misapplied assets, or their equivalent, to the beneficiaries.

[299] For the reasons set out above in discussing the claims of breach of fiduciary duties by Mr Millar, I am satisfied that the assets in question were the subject of fiduciary obligations owed by Mr Millar to First NZ and that Mr Millar had actual knowledge, or was wilfully blind ("shutting one's eyes to the obvious and thus can fairly be equated with the dishonesty involved when there is actual knowledge"[56]) that the assets were received by ISL in breach of fiduciary duty. Mr Millar was the person who was responsible for effecting the transfer of the assets.

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54 At [40].

55 At [38]–[40] (footnotes omitted).

56 *Westpac New Zealand Ltd v MAP and Associates Ltd* [2011] NZSC 89, [2011] 3 NZLR 751 at [27].

[300] However, there is a difficulty with the third element of the claim. While there is no doubt that ISL received the amounts in question it is far less clear that Mr Millar himself can be said to have "beneficially received" the funds for the purpose of this claim.

[301] In one of the authorities relied on by Mr Millar, *Scott v ANZ Bank New Zealand Ltd*, the High Court emphasised that "liability for 'knowing receipt' is receipt-based". That case, as with many of the other authorities on knowing receipt, related to the receipt of funds by the bank. In *Scott* the bank argued it did not "receive" the plaintiffs' funds because it did not receive a net benefit from the funds; the plaintiffs argued the bank did receive a benefit by applying funds to reduce the client's indebtedness. Mallon J was not persuaded that a strike-out application could not succeed in these circumstances.

[302] The question for this court is whether the banking analogy, as in *Scott*, can properly be applied to Mr Millar's position. As detailed above, the shares in ISL were held by the Kaiuma Family Trust. Mr Millar's children are beneficiaries of the Trust. Mr Millar earned his income, or a large portion of it, from ISL. ISL accounts record his salary and also "shareholders' drawings" which Mr Millar acknowledged may have been payments to him. As ISL's financial position improved, so did his. However, Mr Millar did not personally receive the funds First NZ seeks to recover.

[303] In those circumstances I am not persuaded that the knowing receipt claim can succeed against Mr Millar.

***Unjust enrichment***

[304] First NZ submits that both Mr Millar and ISL were unjustly enriched and should not retain the benefit of the monies paid to ISL. The monies it refers to are the excess property management fees, the disclosed property management fee, and the gain fees for the Kilmore Street and Symonds Street properties.

[305] The claim against Mr Millar proceeds on that basis that at all material times he was a "beneficial shareholder in ISL" and was himself enriched.

[306] Both defendants deny the unjust enrichment claims against them. ISL says all payments received by it were legitimately made and received under the First NZ Management Agreement.

[307] To establish unjust enrichment, First NZ must show:[57]

(a) Mr Millar and ISL were enriched by the receipt of a benefit. The enrichment must be quantifiable in monetary terms and should be assessed objectively, with reference to market value;[58]

(b) that enrichment is at the expense of First NZ; and

(c) the retention of the enrichment would be unjust.

[308] About the third element, the High Court in *Torbay Holdings Ltd v Napier* said:[59]

> The law recognises certain categories of cases in which it is considered to be unjust for the claimant to retain the benefit of the money. In the case of a benefit obtained through wrongdoing, the wrongdoer's enrichment at the expense of the claimant is clearly seen as unjust. The unjust factor can be conceptualised as the transferring party's ignorance of a transaction, or the transferring party's actions being outside of their authority, but on either view the taking of an asset without permission, and passing it on to a third party creates the necessary unjustness for an unjust enrichment claim.

[309] As I have found, the First NZ Management Agreement did not entitle ISL to charge First NZ for property management services in addition to the management fee provided for in the Agreement. Similarly, the agreement that governed the parties' relationship after the sale of the last of First NZ Properties.

[310] I do not therefore accept the argument for ISL that it had a contractual entitlement to receive the amounts specified at [304] above.

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57 *Gillies v Keogh* [1989] 2 NZLR 327 (CA) at 332, 341, 342 and 351; and *National Bank of New Zealand Ltd v Waitaki International Processing (NI) Ltd* [1997] 1 NZLR 724 (HC) at 728, affirmed in *National Bank of New Zealand Ltd v Waitaki International Processing (NI) Ltd* [1999] 2 NZLR 211 (CA) at 215.

58 See Tessa Cooksley "The Role of Unjust Enrichment in New Zealand" (LAWS520 Dissertation, Victoria University of Wellington, 2018) at 32, citing Jessica Palmer "Restitution" (2016) 2 NZ L Rev 435 at 442.

59 *Torbay Holdings Ltd v Napier*, above n 35, at [168].

[311] I accept that ISL was enriched at the expense of First NZ. As Woolford J characterised it in *Torbay Holdings*,[60] in this case too, the unjust factor can be conceptualised as the transferring party's ignorance of the transaction. As I have found, Mr Millar was effectively controlling both First NZ and ISL in relation to the transactions in question. There was no adequate disclosure to First NZ of the payments.

[312] As to Mr Millar, the same difficulty arises as in relation to the knowing receipt claim — that is, in establishing that Mr Millar was himself enriched. I am not satisfied that requirement is made out.

[313] I accept the defendants' submission that First NZ is not entitled to the total amount claimed. It paid ISL a property management fee and it received property management services. As in the breach of contract and negligence claims against ISL, the loss and therefore the unjust enrichment comprises the excess property management fees and the gain fees.

**Superstore Properties Ltd**

***Superstore claims***

[314] As with the claim by First NZ, Superstore asserts breach by Mr Millar of his fiduciary duties to the company, and breach of his duties under ss 131 and 137 of the Companies Act.[61] Those breaches arose from his position of conflict, being at all material times a director of Superstore, as well as a director of ISL. Superstore's allegation of knowing receipt is made against both Mr Millar and ISL.

[315] Superstore claims two amounts:

(a) $11,449 plus GST by way of "excess property management fees" paid by Superstore to ISL in the period 1 April 2005 to 31 March 2009. Mr Millar has agreed to pay this sum, but without admission of liability.

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60 At [168].

61 Mr Millar was not a director of Superstore in the relevant period and no claims are made against him by Superstore.

(b) $796,176.26 plus GST paid by Superstore to ISL in the period 1 April 2006 to 31 December 2020, less fees of $151,231.00 paid by ISL to Gravtec, being a total of $644,945.26.

***Superstore Management Agreement***

[316] The duties and responsibilities of FMIS/ISL under the Superstore Management Agreement included that ISL was to "supervise management of [the Superstore Properties] with the assistance of a professional property manager" and to "manage or arrange the management of the three properties and their leasing".

[317] In consideration of the performance by ISL of its duties and responsibilities under the Superstore Management Agreement, the Agreement provided for ISL to charge a management fee calculated at 0.75 per cent of the net capital value of the property (management fee). The evidence is that this fee was charged by ISL to Superstore and that Superstore paid the fee. Superstore does not assert that there was a split of the management fee, into investment management and property management components, as in relation to First NZ.

[318] Franklin was the property manager of the Superstore Properties until 31 December 2003. Under the Superstore Franklin Agreement, Franklin received a fee equivalent to three per cent of the gross rentals received in relation to the three Superstore properties.

[319] Superstore says that ISL was obliged to meet property management fees from within the management fee. This is what occurred while the Superstore Franklin Agreement was in place — the total of the fee incurred by Superstore, including both ISL's management fee and Franklin's fee, amounted to 0.75 per cent of the net capital value of the Superstore Properties.

[320] Superstore says that, when Franklin was undertaking the property management, the arrangement worked as follows:

(a) Payment by Superstore to ISL as the investment manager of 0.75 per cent of the net capital value of the Superstore Properties;

(b) ISL supervision of the property management company, Franklin, with a remuneration to Franklin of three per cent of gross annual rentals;

(c) Franklin received the rentals from the tenants, took its three per cent, and passed the balance of the rental income to Superstore.

(d) Superstore then paid ISL the balance of the management fee (that is, 0.75 per cent of net capital value, less Franklin's fee).

[321] Except between November 2005 and July 2009, in relation to one tenant, the question of Opex payments does not arise in relation to the Superstore claims: the tenants of the Superstore Properties did not pay property management fees as part of their outgoings under their leases with Superstore.

[322] Following termination of the agreement with Franklin in December 2003, Agreement ISL continued to charge Superstore the management fee.

[323] ISL itself took over as property manager for Superstore, with David Penrose fulfilling that function as in-house property manager, from November 2003 to March 2007. From April 2007 to August 2010 Mr Penrose's company PPML was engaged on contract to provide property management services.

[324] From October 2011 Gravtec was contracted to Superstore for its property management function. Gravtec fees were paid by Superstore, and ISL then reimbursed Superstore.

[325] In addition, in the period 1 April 2005 to 31 March 2009 ISL charged and was paid "property management fees" of $11,449.26 plus GST. Superstore says there was no contractual basis for the payment — it was not authorised by the Superstore Management Agreement, nor was there any other contractual entitlement. The payment was not disclosed to shareholders. Mr Millar's evidence was that he had not been able to ascertain what this fee related to and he has agreed to repay this amount, without admission of liability.

[326] In the period 1 April 2006 to 31 December 2020 ISL continued to allocate a fee of three per cent of annual gross rentals to the property management function (being the amount previously paid to Franklin for the provision of property management services). It did so notwithstanding that the actual cost to it of providing those services was substantially less than three per cent of gross rentals (both when Mr Penrose/PPML were providing the service and when Gravtec was providing the service). Mr Prendergast calculated the difference between what Gravtec was paid and three per cent of the gross rentals for each of the years 2012 to 2021. By way of example, in the 2013 financial year Gravtec was paid $11,400.00; three per cent of the gross rentals amounted to $57,474.15.

[327] That gives rise to Superstore's second claim, which is for $796,176.26 plus GST, being a notional amount based on the amount that Franklin would have been paid (three per cent of gross rentals) if it had been managing the Superstore Properties in the period the subject of the claim and thus it says, the "bonus" amount that ISL took for itself, when it was not actually providing property management services. From that figure Superstore deducts $151,231, being the amount paid by ISL to Gravtec, to arrive at a total claim of $644,945.26 plus GST and interest.

[328] The first and second defendants acknowledge that ISL continued to receive the 0.75 per cent net capital value management fee throughout, but assert ISL's contractual entitlement to that fee. They say the Superstore Management Agreement required ISL to supervise the management of the Superstore Properties "with the assistance of a professional property manager" and, in return for performing its duties and responsibilities under the agreement, entitled it to the management fee. From the time of Superstore's incorporation, those property management services were always provided, and ISL always met the costs of property management from the management fee — first the costs of property management provided by Franklin, and then the services provided by Gravtec. That is what it had contracted to do.

[329] The defendants say that is supported by the plaintiffs' own evidence. Mr Osborn, a forensic accountant who gave expert evidence for the plaintiffs, accepted that all property management services provided to Superstore were paid by ISL. Mr Murray's evidence as an independent director of the plaintiff companies did not

address the claim. Mr Prendergast, also a director of the plaintiff companies, accepted in cross-examination that ISL always met the costs of Superstore’s property management from the management fee of 0.75 per cent of net capital value paid by Superstore to ISL.

[330] The first and second defendants also say that the amount claimed by Superstore is not representative of either Superstore’s loss or any benefit to Mr Millar and ISL. The notional costs that Franklin would have been paid in a period when it was not providing property management are not recoverable from Mr Millar or ISL under any of the grounds alleged. ISL, and then Gravtec, managed the Superstore Properties from the time of Franklin's termination, at ISL’s cost. That is, ISL did in fact meet the costs of Superstore’s property management.

***Discussion***

[331] The essence of Superstore’s claim is that the cost to ISL of contracting Gravtec to provide property management services was substantially less than the amount ISL continued to receive by way of its 0.75 per cent management fee under the Superstore Management Agreement.

[332] As a consequence, ISL retained a greater proportion of the 0.75 per cent of net capital value management fee paid to it by Superstore than it did when Franklin was carrying out the property management services. However, despite Mr Millar’s clear conflict of interest, he and ISL did not disclose this changed situation to Superstore.

[333] In an arm’s length arrangement ISL might be entitled to rely on its agreement with Superstore to maintain a claim to the full 0.75 percent management fee. This was not an arm’s length arrangement.

[334] I have set out the nature of the relevant fiduciary duties and the circumstances giving rise to Mr Millar’s position of conflict, in the context of the analysis of the claims by First NZ. That analysis is equally applicable to the Superstore claim.

[335] Mr Millar was a director of both Superstore and ISL; he derived his livelihood from ISL. Mr Millar had placed himself in a position where his duties to Superstore

and his personal interests conflicted. He was in breach of his fiduciary and statutory obligation to act in good faith and in the best interests of Superstore. He also breached his duty not to profit from his position as a director and not to act for his own benefit, or the benefit of a third party (ISL) without the informed consent of his principal. He did not obtain that informed consent. As Mr Abernethy, an expert witness for the defendants, accepted, if there was a change in the company's contractual arrangements that benefited a director, that should be disclosed to the shareholders. Mr Millar did not disclose the changed situation and seek Superstore's consent to the post-Franklin arrangement.

[336] On the contrary the agreement between Superstore and Gravtec was backdated by some six years. The fees paid to Gravtec were not disclosed in Superstore's Annual Accounts until 2020. It is not enough to say, as the first and second defendants do, that the fact that ISL was being remunerated by Superstore for providing services to it was "in plain sight" in that in all relevant years the fee paid to ISL was disclosed in the annual reports. That is not disputed. The first and second defendants rely on the fact that the management fee was paid and charged on terms which were unaltered since the time Superstore was incorporated in 1999 and from the fee ISL and its predecessor had always funded the costs of Superstore's property management. But that highlights the crux of the problem: the management fee did not change and the provision of property management services to Superstore continued, but the cost to ISL had been significantly reduced, and hence ISL's margin significantly increased, by virtue of the changed contractual arrangements. And that change in position was not advised, or consented, to by Superstore.

[337] I conclude that Mr Millar's failure to disclose the changed situation and the increased amount being received by ISL post-Franklin, after payment of fees for third party property management, was a breach of Mr Millar's fiduciary duties and of his obligations under s 131 of the Companies Act.

[338] The analysis of s 137 set out above in relation to the First NZ claim applies to the Superstore claim also. Mr Millar took no steps to explain or review the nature of the payment for Superstore's property management services after termination of the

Superstore Franklin Agreement, or at any point. A reasonable director would have done so for. I conclude that Mr Millar was in breach of his obligations under s 137.

[339] Superstore also alleges that the amount of $644,945.26 plus GST is recoverable from Mr Millar and ISL by way of a knowing receipt claim. ISL received that amount knowing that, in directing payment of it, Mr Millar was in breach of his fiduciary and statutory duties to Superstore.

[340] As to the knowing receipt claims against Mr Millar, the analysis of the requirements to sustain a knowing receipt claim are set out above in the context of the First NZ claim.

[341] There is no evidence of personal receipt by Mr Millar of the amounts claimed. But I accept that Superstore has a knowing receipt claim against ISL. Mr Millar owed Superstore fiduciary obligations in relation to the management fee. ISL received the management fee. Mr Millar was in effect ISL. In those circumstances I conclude that ISL received or retained the amount claimed with actual knowledge that Mr Millar, in directing the payment or retention to ISL, was in breach of his fiduciary duties to Superstore and that therefore ISL had no lawful entitlement to the amount claimed.

[342] Superstore has calculated the appropriate remedy on the basis that ISL continued to receive, and Superstore continued to pay, 0.75 per cent of the net capital value of the Superstore Properties, when ISL was paying substantially less for the property management function than the three per cent of gross rental income it continued to allocate in its books. Superstore's loss is that margin — that is, what Franklin would have been paid, less the fee paid to Gravtec. I accept that is the appropriate calculation. It is representative of Superstore's loss arising from Mr Millar's breach of his fiduciary and statutory duties to the company, in failing to disclose the details of the changed property management arrangement (post-Franklin), including the substantial financial benefit to ISL, and seek informed consent to those arrangements.

[343] In conclusion in relation to Superstore's claims, I accept that there was no contractual or other basis for the payment of $11,449.26 plus GST and Superstore is entitled to judgment against Mr Millar and ISL for that amount.

[344] I have also found that Mr Millar directed the continued payment to ISL of the management fee in breach of his fiduciary duties and his obligations under ss 131 and 137.

[345] Superstore is entitled to judgment against ISL for:

(a) $11,449.26 plus GST.

(b) $644,945.26 plus GST (being the disclosed property management fee, less $151,231.00 paid to Gravtec).

[346] Superstore is entitled to judgment against Mr Millar for:

(a) $11,449.26 plus GST.

(b) $644,945.26 plus GST (being the disclosed property management fee, less $151,231.00 paid to Gravtec).

**Springs Road Property Ltd**

[347] Springs Road claims against all three defendants — against Mr Millar and Mr Mephan for breach of their fiduciary and ss 131 and 137 Companies Act duties, and against Mr Millar and ISL for knowing receipt. The total claim is for $517,959.26 plus GST.

***Springs Road Management Agreement***

[348] The Springs Road Management Agreement provided for ISL to charge a management fee calculated at 0.5 per cent of the net capital value of the Springs Road property, payable monthly in arrears (management fee).

[349] The Agreement required ISL to "supervise the management of the Property with the assistance of a professional property manager".[62] The Springs Road Property did not change during the course of the agreement.

[350] The Agreement did not split the management fee into an investment management fee and a property management fee. This fee was charged by ISL and paid to it by Springs Road.

[351] Under the Springs Road Franklin Agreement, Franklin provided the property management services from January 1998 until ISL terminated the agreement on 31 December 2003.

[352] Springs Road says the Springs Road Franklin Agreement illustrates the bargain that Springs Road contracted for with ISL:

(a) ISL was paid 0.5 per cent of the net capital value of the Springs Road Property (management fee), as investment manager;

(b) ISL was to supervise a professional property manager (Franklin) with Franklin receiving its remuneration at a rate of four per cent of gross annual rentals; and

(c) Springs Road tenants met the costs of the property management function provided by Franklin, by way of their Opex payments under the leases.

[353] Following the termination of the Springs Road Franklin Agreement, ISL assumed the role of property manager for Springs Road and Mr Penrose fulfilled that function as the "in-house property manager" until 2007. From 2007 until October 2011 Mr Penrose's company, PPML, was contracted by ISL to fulfil the property manager role. From October 2011 ISL contracted Gravtec to undertake the property management function.

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[62] Clause 3.3.

[354] In summary, Springs Road's claim is that, following termination of the Springs Road Franklin Agreement, it paid property management fees, in addition to the management fee:

(a) It paid ISL a further fee in the period 1 April 2006 to 31 December 2020 (totalling $371,822.63 plus GST), purportedly for property management services, as "Opex management" (Opex management fee). However, when a property was tenanted, Springs Road charged its tenants an amount equal to the property management fees, as part of operating expenses for the property; and

(b) For the period 1 April 2011 to 31 March 2020 Gravtec was separately contracted and was paid $146,136.63 plus GST to undertake the same property management service, where Gravtec's fees were met from Opex paid by Springs Road's tenants. Springs Road says ISL failed to disclose Gravtec's involvement.

[355] These additional fees totalled $517,959.26 plus GST.

[356] Springs Road says there was no contractual basis, whether in the Springs Road Management Agreement or elsewhere, for ISL to charge a fee for property management in addition to the management fee it was receiving under the Springs Road Management Agreement.

[357] Springs Road also says that ISL contracted Gravtec to undertake the same property management function for which ISL was charging the management fee. Gravtec's fees were paid under a written agreement dated 20 November 2017 between Gravtec and Springs Road. The defendants backdated that agreement to cover property management services provided by Gravtec from 1 October 2011. Springs Road says that, as for the First NZ and Superstore arrangements with Gravtec, Mr Millar's explanation of the backdating of the agreement lacks credibility and was an artifice which had the effect of avoiding disclosure of the agreement. The Gravtec arrangement was not disclosed to Springs Road shareholders, except for the payments

made in the period 1 April 2018 to 31 March 2020, which were disclosed in the 2020 Annual Report.

[358] Springs Road claims against Mr Millar and Mr Mephan for breach of their fiduciary duties and duties under ss 131 and 137 of the Companies Act, in allowing a situation where ISL continued to receive its 0.5 per cent management fee, but also charged Springs Road an additional "Opex" management fee, while Gravtec was in fact providing the property management services. Springs Road also claims against Mr Millar and ISL for knowing receipt. It seeks the total amount of $517,959.26 plus GST from Mr Millar and ISL and from Mr Mephan it seeks $79,496.04 plus GST (being Springs Road's alleged loss and/or Mr Mephan's benefit for the period 1 April 2018 to 31 March 2020, when Mr Mephan was a director of Springs Road).

[359] The defendants' response is, first, that the Gravtec fees were not paid by Springs Road, but by its tenants. Second, there has been no failure to disclose the payments under the Companies Act. The allegation that fees were paid without lawful authority cannot be sustained, because Springs Road's Constitution permitted Mr Millar to participate in decision-making about payment of the fees, despite having an interest in the payments. Finally, the fees were paid for services provided to Springs Road by ISL, following Franklin's termination, and which were necessary and in addition to ISL's management obligations under the Management Agreement.

[360] As to the last point, the defendants say that the property management service ISL was providing, and for which Springs Road was paying, from 1 April 2006 to 31 December 2020 was not the same service that Gravtec was providing. Rather it was "Opex management" which had previously been carried out by Franklin but was not part of Gravtec's services. It was in addition to the services provided by Gravtec.

[361] The defendants rely on evidence from Mr Penrose, the owner/operator of PPML, who was employed as ISL's inhouse property manager from November 2003 to March 2007. He says that, in that role, he was responsible for managing Opex obligations for both First NZ and Springs Road. Mr Penrose listed his responsibilities in the role.

[362] In addition, the defendants say that the amount sought by Springs Road in relation to Gravtec ($146,136.63 plus GST) has not in fact been incurred by Springs Road, having been funded by the tenants of the Springs Road Property, in accordance with the terms of their leases, through their Opex payments (meaning there is no loss to Springs Road) and received by third parties (meaning there is no benefit to the defendants). These were arm's length transactions for legitimate property management services, provided on behalf of Springs Road.

[363] As to the allegation of non-disclosure, as with the First NZ claim, the defendants rely on subs 140(2) of the Companies Act to submit that general disclosure was sufficient. This took the form of general disclosure in all annual accounts that all transactions between Springs Road and ISL were related party transactions and transactions in which Mr Millar had an interest.

[364] Further, the defendants say that the fees were able to be approved by Mr Millar as an interested director because Springs Road's constitution specifically provides that an interested director is able to authorise transactions in which he or she has an interest.

[365] The defendants agree that the fees did not appear in Springs Road's Annual Accounts, but say this was not a failure of disclosure in accounting terms. The fees did not appear in the Annual Accounts because they were not revenue, costs or expenses of Springs Road and had no bearing, whether positive or negative, on Springs Road's equity position which is required to be described in the Annual Accounts.

[366] Accordingly, the fees cannot be said to be "undisclosed" in breach of the defendants' obligations.

***Discussion***

[367] The Springs Road Management Agreement is in substance the same as the First NZ Management Agreement. As for First NZ, I do not think the defendants can rely on cl 3.9 ("… instruct such … other consultants or advisers as [FMIS] deems necessary …") in the face of cl 3.3 which specifically states FMIS is to "supervise the management of the Property with the assistance of a professional property manager". And, as discussed in relation to the First NZ Management Agreement, the purpose of

cl 4.1 is to protect ISL from being held liable to third parties separately as a principal. It is predicated on ISL as agent properly incurring a liability to a third party. It does not apply to ISL's first party liability to Springs Road if it acts outside the terms of their agreement.[63]

[368] As with First NZ, I conclude that ISL was required to provide Springs Road's property management services from within the management fee.

[369] ISL says the service it provided was in addition to the property management services provided by Gravtec. But, although Mr Penrose listed the responsibilities he assumed as ISL's in-house property manager, he did not explain the alleged "gap" between the property management services previously provided by Franklin, and those services included in his role or, subsequently, Gravtec's role.

[370] Mr Mephan's description of ISL's "supervision" of the property management function also indicated it was very limited. He acknowledged that ISL was able to rely on Terra Firma for most day-to-day tasks, maintaining only an "overarching function". Gravtec did most of the actual property management. Mr Mephan acknowledged Richard Eberlein of Gravtec as "an important part of the fabric of what was being done". To the extent that ISL did provide supervision, that was through Mr Barnes, Mr Millar and Mr Mephan. Mr Mephan acknowledged that none of those three were property management experts, and they relied on Gravtec and Terra Firma as the experts. From Mr Mephan's evidence ISL's role was limited to paying the Opex accounts, banking, and maintaining files and accounting records.

[371] I conclude that ISL did not undertake any material property management services for Springs Road from 2011, as those services were delivered by Gravtec.

[372] Nor was there a contractual basis for ISL to charge a fee in addition to the management fee and the fee paid to Gravtec. I accept that the Springs Road Management Agreement did not distinguish between property management and investment management. The fee of 0.5 per cent of the net capital value of the Property was a global fee to be paid "[i]n consideration of the performance by [ISL] of its duties

63 Gault, above n 4, at [19.5.2].

and responsibilities under this Agreement". Those included "supervise the management of the Property with the assistance of a professional property manager". The activities that Mr Mephan described seem to me to fall within that description.

[373] I accept that the backdating of the Gravtec agreement was an artifice. The lack of transparency about the arrangement was compounded by the fact there was no disclosure of the Gravtec agreement to Springs Road shareholders until the 2020 Annual Report. The practical effect was that no questions were or could be asked by shareholders about the various amounts Springs Road was paying for the provision of property management services.

[374] I do not accept the defendants' submission that general disclosure was sufficient, for the reasons set out in relation to First NZ above.

[375] As discussed in relation to the Superstore claim, while it is possible that, in an arm's length/independent directors' arrangement, Springs Road might have agreed to an Opex management fee, in addition to the management fee, that was not the situation here. This was not an arm's-length arrangement.

[376] Mr Millar had placed himself in a position where his duties to Springs Road and his personal interests conflicted. He was in breach of his fiduciary and statutory obligations to act in good faith and in the best interests of Springs Road. He also breached his duty not to profit out of his position as a director and not to act for his own benefit, or the benefit of a third party (ISL) without the informed consent of their principal. Mr Millar did not disclose the changed situation and seek Springs Road's consent to the post-Franklin arrangement. That would have required an explanation as to the gap between the services provided by Franklin and what was subsequently thought necessary. It would also have required disclosure of the Gravtec agreement at the time it was entered into, so that shareholders were aware of the totality of the arrangements.

[377] On the contrary the agreement between Springs Road and Gravtec was backdated by some six years. The fees paid to Gravtec were not disclosed in Springs Road's Annual Accounts until 2020.

[378] I accept that, notwithstanding the lack of disclosure, the fee paid to Gravtec was covered by the Opex paid by the tenants, as it had been when Franklin provided property management services. It is clear that the property management services were in fact provided by Gravtec. The amount of $146,136.63 GST is not therefore a loss to Springs Road, or a benefit or profit to ISL.

[379] However, the additional Opex property management fee paid to ISL itself was not authorised by the Springs Road Management Agreement or any other agreement, does not appear to have been for any meaningful service additional to that provided by Gravtec. It was not adequately disclosed. As I have concluded above, the lack of disclosure was compounded by the backdating of the Gravtec agreement.

[380] I conclude that Mr Millar was in breach of the fiduciary and s 131 Companies Act duties he owed to Springs Road. He was in a position of conflict for the reasons already discussed in relation to the First NZ claim. Despite that conflict, he failed to disclose the changed situation and the increased amount being received by ISL post-Franklin, after payment of fees for third party property management, and seek Springs Road's informed consent to the new arrangements. I also conclude he was in breach of his obligations under s 137 to act as a reasonable director would have done. The context and the nature of the breaches are as analysed in relation to the First NZ and Superstore claims.

[381] As with the First NZ claims, I find that Mr Mephan's position was different from Mr Millar's. As noted earlier, Mr Mephan was not a director of ISL. Unlike Mr Millar, he did not have effective power of appointment of the plaintiff companies' directors. Mr Mephan had no role with the property companies during the period of the Franklin Agreements. The agreement with Gravtec had been in place well before Mr Mephan was appointed a director on 13 February 2018 — the contract took effect from1 April 2011 (with the backdated contract being signed on 21 November 2017).

[382] As I concluded in relation to First NZ, Mr Mephan undoubtedly owed fiduciary and s 131 duties to Springs Road and was in a position of potential conflict, given he was a director of the property companies and his income derived from ISL. However, Mr Mephan lacked the knowledge necessary to understand that the property

management arrangement entered into with Gravtec was not in Springs Road's best interests, having regard to what I have found was the longstanding nature of that agreement. As already discussed, it is also relevant that Mr Millar had control of the banking arrangements for the property companies.

[383] For those reasons, I accept that, in terms of s 131 of the Companies Act, Mr Mephan may have had a genuinely held and reasonable belief that he was acting in the best interests of Springs Road.

[384] Taking all of these factors into account, I conclude that in relation to the claims against him in relation to the payment to Gravtec, Mr Mephan did not act in breach of his fiduciary or s 131 duties, or carelessly in breach of s 137.

[385] By a finer margin, I conclude that the same is true in relation to the Opex management fee paid to ISL. That too had been in place for a considerable period (12 years) before Mr Mephan's appointment, apparently without any issue having been raised about the payment. As above, Mr Millar had control of the banking arrangements for the plaintiff companies, so Mr Mephan would not have had full visibility of the totality of the payments being made by Springs Road for property management services.

[386] As to the knowing receipt claim, there was no evidence of personal receipt by Mr Millar of the funds claimed. However, the requirements of a knowing receipt claim against ISL are made out. It is not disputed that ISL received the $371,822.63 plus GST, for Opex property management.

[387] Springs Road is entitled to recover from ISL the $371,822.63 plus GST for Opex property management fees paid to ISL.

[388] Springs Road is entitled to recover from Mr Millar the $371,822.63 plus GST for Opex property management fees paid to ISL.

**Notices to Avoid**

[389] All three plaintiff companies say that they issued notices to Mr Millar and ISL under s 141 of the Companies Act, declaring the avoidance of the payments claimed as being interested director transactions at the time those payments occurred. No repayment has been made by any defendant of those transactions.

[390] The first and second defendants say any claim to avoid the transactions on s 141 grounds would have had to be specifically pleaded, so that issues of fair value arising under subss 141(3), (4) and (5) could be addressed in evidence. It was not. The plaintiffs cannot use the s 141 notices to secure relief under the causes of action advanced because of subs 141(6) which says "A transaction in which a director is interested can only be avoided on the ground of the director's interest in accordance with this section or the company's constitution."

[391] No submissions were made before me about s 141 so I do not discuss this issue further.

**Counterclaims**

[392] ISL counterclaims against each of the property companies.

***Repudiation***

[393] On 31 December 2020 Mr Millar wrote to the directors of the three plaintiff companies, saying:

> You have asked ISL to make various payments to facilitate the undertaking by a new company of the management services currently provided to the property companies by ISL. This is despite ISL having ongoing rights and responsibilities under the existing management agreements and without any agreement having been reached for the termination of ISL's rights and responsibilities under those agreements. You have also, on behalf of the new management companies or the property companies, solicited an existing ISL employee and the party with whom ISL has an existing contractual arrangement for the provision of property management services.
>
> Your conduct on behalf of the property companies is effectively a repudiation of the management agreements which are currently in place. On ISL's behalf, I give notice of cancellation of the management agreements ISL has with each

> of the property companies on account of the property companies' repudiation (through your actions).

[394] ISL relies on that purported repudiation of the management agreements and seeks recovery of the profits that it says it would have received (quantifying a one-year notice period) had the property companies cancelled the management agreements on notice.

[395] ISL relies on s 36 of the Contract and Commercial Law Act 2017:

> **36 Party may cancel contract if another party repudiates it**
>
> (1) A party to a contract may cancel the contract if, by words or conduct, another party (**B**) repudiates the contract by making it clear that B does not intend to—
>
> (a) perform B's obligations under the contract; or
>
> (b) complete the performance of B's obligations under the contract.
>
> (2) This section is subject to the rest of this subpart.

*ISL's submissions*

[396] ISL says there was a pattern of conduct by the property companies, beginning in October 2020 and continuing until 31 December 2020, which amounted to repudiation of the management agreements. Through the actions of Mr Murray and Mr Prendergast, the new, independent directors, who made it clear that, as directors of the property companies, they intended to either establish an in-house property management company or contract another investment manager, without terminating the management agreements in accordance with their terms (a year's notice in case of First NZ and Springs Road and two years' notice in the case of Superstore).

[397] The conduct on which ISL relies is:

(a) In October 2020, Mr Murray and Mr Prendergast were engaging with other parties, including Colliers and MAAT Consulting, ISL says, about those parties providing management services to the plaintiffs in substitution for ISL.

(b) Mr Murray and Mr Prendergast developing an internal model for "bringing the management of the companies in house".

(c) The plaintiff companies establishing a management company, FSS Management Ltd (FSS) on 9 December 2020, to replace ISL, without communicating with Mr Millar and ISL, and opening bank accounts in the name of FSS.

(d) FSS employing Richard Eberlein, the principal of Gravtec, on 15 December 2022 as its Property Manager, and failing to advise Mr Millar that FSS had secured Mr Eberlein's services.

(e) The plaintiffs entering into a shareholders' agreement in respect of FSS, on 17 December 2020, and failing to advise Mr Millar or ISL.

(f) FSS employing Paul Rosanowski (who was employed by FSS on about 15 December 2020) to assist with the transfer of investment management services from ISL to FSS.

(g) Mr Murray and Mr Prendergast requiring that ISL make payments of capital to the plaintiffs, in the Christmas period, so that FSS could meet its start-up and ongoing costs.

(h) Mr Murray and Mr Prendergast approaching and soliciting Kathryn Brownlie (who was then an employee of ISL) in December 2020.

(i) FSS, in December 2020, undertaking obligations which ISL had been contracted to provide.

*Plaintiffs' submissions*

[398] The plaintiffs' response is that, as a matter of law, the actions relied on by ISL cannot amount to repudiation, which requires an irrevocable indication that a party will not perform its contractual obligations.

[399] The property companies' primary obligation under the management agreements was to pay ISL a fee for the services provided by ISL. There is no evidence or suggestion of any intention not to perform that obligation. Mr Murray's evidence was that the property companies were ready, willing and able to pay ISL its management fee. The property companies did in fact continue to pay ISL its fee, up to and including the date of cancellation by ISL.

[400] Second, the plaintiffs say, that as a matter of fact they did not repudiate the management agreements.

[401] From May 2020, ISL had agreed to assign the management agreements between ISL and each of the property companies to PPML (Mr Penrose's company) and (at Mr Millar's behest) the parties were discussing the terms of a mutually agreed transition after PPML withdrew from the negotiations with the property companies.

[402] In addition, the property companies had serious concerns over ISL's ability to carry out its property management obligations.

[403] The first of those concerns related to insurance. ISL was unable to obtain insurance for itself, or the property companies, which was previously held under a policy headed by ISL. When Vero Liability, which had previously insured ISL and the property companies, learned of the fraud committed against the property companies by Mr Barnes, through ISL, and the allegations raised by a third party of mismanagement by ISL, it decided not to renew the policies. Vero notified ISL of its decision on 11 November 2020, with effect from 15 December 2020.

[404] This meant that ISL, the property companies and their directors were uninsured. It also meant the property companies were in breach of their agreements with Richard Eberlein who was providing property management services directly to the property companies through his company Gravtec. It was a requirement of the contracts between Gravtec and the property companies that the property companies hold insurance for the benefit of Gravtec.

[405] ISL decided not to apply for alternative insurance and advised the property companies of this on 24 November 2020.

[406] Mr Eberlein was critical to the ongoing operations of the property companies. ISL's refusal to obtain insurance jeopardised his ongoing involvement. As a result, the directors approached Mr Eberlein to ensure his ongoing involvement with the property companies. They did not "poach" him — he was not employed or engaged by ISL, but contracted through his company directly to the property companies. In any event, the approaches were a direct consequence of, and necessitated by, ISL's failure to obtain insurance.

[407] The plaintiffs' second concern related to the ISL management. By late 2020 the Property companies had concerns over ISL's ability to discharge its management obligations. The inability and/or refusal to obtain insurance occurred in November 2020. Subsequently, on 9 December 2020, David Penrose stepped down as ISL's CEO and advised ISL and Mr Murray and Mr Prendergast of that (with four working days' notice). There was no obvious transition. Mr Murray asked Mr Millar on 11 December 2020 to clarify how ISL would then fulfil its management obligations. On 17 December 2020 Mr Millar provided a bare assurance that ISL's obligations would continue to be met. This was unsatisfactory for Mr Murray who asked for details of Mr Penrose's "to-do" list. Mr Millar did not provide a clear answer.

[408] Third, as above, ISL and the property companies were in discussions about a mutually agreed and orderly transition of management functions from ISL to FSS. The plaintiffs say they were open to discussing any issues ISL had with the relationship, if a mutually agreed transition was not agreed.

[409] As to engaging staff, the plaintiffs say Kathryn Brownlie remained employed by ISL through until July 2021 and was not offered employment in December 2020. Paul Rosanowski was not employed by or contracted to ISL. Neither Ms Brownlie nor Mr Rosanowski gave evidence at the hearing.

[410] The plaintiffs say that, as in *HEB Contractors Ltd v Verrissimo*,[64] the Court must consider the "total position". From May 2020 ISL had agreed to assign the management agreements. The steps taken by the property companies in setting up FSS, approaching key personnel, obtaining insurance and directing Mr Millar to process payments, were all taken in preparation for the anticipated orderly transition of the management function and to ensure that in the meantime the management function continued to be performed. The plaintiffs say those steps were to ensure that ISL's management obligations continued to be discharged in the face of ISL's failure to do so.

[411] In any event, as set out above in relation to the question of insurance, ISL was not ready, willing and able to perform its obligations under the management agreements.

[412] Following ISL's refusal to obtain insurance, the directors of the property companies applied for insurance. In order to do so they needed to establish a new entity. This was the reason they established FSS on 9 December 2020.

[413] On 24 December 2020 ISL was directed to advance funds from the property companies to FSS. It refused to do so, Mr Millar noting he was concerned that there was no contractual relationship with FSS. The reason for the advance was to allow FSS to pay for the insurance which the directors had managed to obtain. This was explained to Mr Millar. On 20 December 2020 ISL refused to process a payment as directed.

[414] On 23 December 2020 one of First NZ's subsidiaries, Symonds110 Ltd, was served with draft High Court proceedings. Mr Murray twice asked Mr Millar to confirm whether the company's insurers had been notified. Mr Millar did not respond to that question.

[415] The plaintiffs say there was a direct causative link between ISL's defaults and the alleged acts of repudiation that ISL relied on to cancel the agreements.

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64 *HEB Contractors Ltd v Verrissimo* [1990] 3 NZLR 754 (HC).

[416] Nor did ISL raise any concern that the property companies were intending to not perform their obligations — it did not invoke the arbitration provision of the management agreements but instead on New Year's Eve 2020 summarily cancelled the agreement. The plaintiffs say that ISL had no intention to perform its obligations.

*Discussion*

[417] Repudiation requires that one party has made it clear that it would not perform its side of the bargain. In *Betham v Margetts*,[65] the Court held that the test is an objective one:

> The question is whether in all the circumstances the communication should be regarded as an irrevocable indication that the party concerned would take no further steps to perform his or her obligations under the contract or alternatively that he or she would perform it only in a manner substantially inconsistent with the obligations which the contract imposed.

[418] The position was that, as Mr Millar conceded in cross-examination, he had previously had complete control over what occurred between the property companies and ISL. He had now lost that control. I conclude from the evidence that Mr Millar then became defensive and then combative towards the property companies' directors, attempting to thwart their intentions. I accept that Mr Millar/ISL had no intention of continuing to perform ISL's obligations. As detailed above, Mr Millar failed to respond reasonably or in a timely fashion to requests or directions from the new directors of ISL.

[419] Having regard to the overall position, I conclude that the plaintiff companies' actions were taken, initially, with the intention of progressing the outcome agreed between the parties. Then, in the face of Mr Millar's intransigence, to ensure that the plaintiff companies could continue to function.

[420] I do not accept ISL's claim that the Property Companies repudiated their respective Management Agreements, thus entitling ISL to cancel the Agreements.

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[65] *Betham v Margetts* [1996] 2 NZLR 708 (HC) at 3.

## Affirmative defences

### *Indemnity and limitation of liability – ISL*

[421] ISL pleads that it has limited its liability, and is indemnified, in terms of the substantive claims by First NZ against ISL in contract and in negligence. It relies on cls 6 and 7 of the First NZ Management Agreement, which provide:

> **6. INDEMNITY**
>
> 6.1 FMIS shall not in the performance of this Agreement be liable to FPL [Foodstore Properties Ltd] or the Subsidiaries or to any other person for any act or omission negligent tortious or otherwise of FMIS, FPL or any Subsidiary or any agent or employee of any of them and FMIS shall be entitled to be indemnified and saved harmless by FPL and the Subsidiaries from all liabilities, losses, damages, costs or expenses by reason of any of the foregoing acts or omissions.
>
> 6.2 FPL and the Subsidiaries shall save harmless and indemnify FMIS from and against any liability (including liability for taxes), loss, cost, damage or expense that may be incurred or suffered by FMIS howsoever arising relating to the performance by FMIS of its duties and responsibilities under this Agreement.
>
> **7. LIMITATION OF LIABILITY**
>
> 7.1 FMIS shall not be liable for any loss or damage sustained or incurred by FPL or any Subsidiary arising out of or in relation to or on account of any act or omission in the course of or in connection with the performance by FMIS of its duties and responsibilities under this Agreement, for any decline in value of the Properties or any part of them or from the act, omission or default of any property manager appointed by FMIS, or for any other reason whatsoever.
>
> 7.2 Without limiting clauses 6 or 7.1, FMIS shall not be liable for any failure to perform under this Agreement if FMIS is prevented from performing by any present or future statute, regulation, rule, ordinance, bylaw, or action of national or local government, or by any declaration, order or judgment of any court.

[422] ISL also relies on the equivalent of cls 6 and 7 in the Springs Road and Superstore Management Agreements, in materially the same terms, in relation to the knowing receipt causes of action against ISL by Superstore and Springs Road.

[423] The plaintiffs say that while cl 6.1 in the First NZ Management Agreement provided for exclusion of liability (including for negligence) and indemnity, that provision was agreed to in a very different context. ISL had a genuine arm’s-length

arrangement with Franklin, a third party, to provide the property management services to the plaintiff companies. The arrangement was approved by an independent board.

[424] Clause 6.2 contained no reference to tortious liability, therefore negligence was not covered. In any event, it is plainly a third party save harmless/indemnity clause.

[425] Clause 7 is a limitation of liability provision. It contains no reference to negligence or tortious activities, and these are not covered. But further, given the lack of independence of ISL, it cannot have been intended that it have limited liability for the very actions and omissions it procured.

[426] First NZ also says that cls 6 and 7 of the First NZ Management Agreement ceased to exist on the sale of the last property. There was no clear and unambiguous expression by ISL that it wanted full indemnity and exclusion of tortious liability beyond that point. It is not reasonable to imply such draconian provisions.

[427] As Asher J said in *Dorchester Finance Ltd v Deloitte*:[66]

> Given the premise that an exclusion clause will enable a party to escape liability for a breach of a contractual promise, it will be assumed that a party will not have intended to limit liability unless clear and unambiguous language is used. A Court will ordinarily look for clear language or necessary implication before concluding that the right to claim for damages is extinguished. Such an intention will not be lightly attributed. The ultimate objective is to ascertain what the parties intended the words to mean in the particular factual context in which the contract was made.

[428] As I have already found, the written First NZ Management Agreement came to an end in November 2004 and from that point on the relationship between the parties was governed by a new contract. ISL does not plead any "implied term" in relation to exclusion or limitation of liability in tort under the undocumented arrangement from October 2004.

[429] I agree that it would not be reasonable to imply provisions such as cls 6 and 7 into the continuing arrangement between the parties.

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[66] *Dorchester Finance Ltd v Deloitte* [2012] NZCA 226 at [33] (footnotes omitted).

[430] Even if I agreed that there were such implied terms in the continuing arrangement, in my view the wording of those clauses (as in the original Agreement), together with the context, mean that the interpretation sought by the defendants is not available.

[431] Clause 6.1 on the other hand is clearly intended to relate to ISL's own liabilities. The wording of cl 6.1 is that ISL was entitled to be indemnified from all liabilities, losses, damages, costs or expenses *by reason of* ISL's acts or omissions. As the plaintiffs submit, when the clause was inserted in each of the management agreements (1995, 1998 and 1999) the situation involved a genuine arm's-length third party (Franklin) providing property management services, with that arrangement approved by an independent board. To construe the clause to cover the subsequent situation where, as I have found, there was no independent board and Mr Millar was to all intents and purposes ISL and had full control of the property companies, would allow ISL to benefit from its own default. I do not accept that interpretation.

[432] While cl 7 is a limitation of liability provision, it does not refer to negligent or tortious acts or omissions and cannot be read that widely. I accept that it cannot have been that such indemnity was available to ISL when the very acts and omissions that are in issue were procured by ISL.

[433] In addition, as the plaintiffs submit, there was no evidence at trial of these indemnities being entered into the interests registers of the plaintiff companies, in breach of s 162(7) of the Companies Act. The plaintiffs say that this too would void any indemnity given (to the extent that it applied at all, which they deny).

***Deeds of indemnity – Mr Millar and Mr Mephan***

[434] Both Mr Millar and Mr Mephan say they are indemnified against any costs and liability incurred to the plaintiffs, on the basis of the Deeds of Indemnity signed respectively in 1995 (First NZ), 1998 (Springs Road) and 1999 (Superstore). They come within the definition of "Indemnified Person" in each of those Deeds, being a director or former director of the company or a related company.

[435] The deeds are in materially similar terms. The operative clauses are:

2. **INDEMNITY FOR COSTS IN PROCEEDINGS**

Subject to compliance by the Indemnified Person with the requirements of **clauses 5 and 6**, the Company agrees to indemnify that Indemnified Person against any costs which that Indemnified Person incurs in any proceeding:

(a) that relates to liability for any act or omission of the Indemnified Person in the Indemnified Person's capacity as a director or employee, as the case may be, of the Company or a Related Company; and

(b) in which the Indemnified Person is acquitted, or has judgment given in the Indemnified Person's favour, or which is discontinued.

3. **INDEMNITY FOR LIABILITIES INCURRED**

Subject to **clause 4** and to compliance by the Indemnified Person with **clauses 5 and 6**, the Company agrees to indemnify that Indemnified Person against:

(a) any liability the Indemnified Person incurs to any person other than the Company or a Related Company for any act done or omission made in the Indemnified Person's capacity as a director or employee, as the case may be, of the Company or Related Company; and

(b) all costs the Indemnified Person incurs in defending or settling any claim or proceeding relating to such liability.

4. **LIMITATION ON INDEMNITY FOR LIABILITIES INCURRED**

An Indemnified Person shall not be indemnified under **clause 3** where the liability of the Indemnified Person is:

(a) criminal liability; or

(b) where the Indemnified Person is a director, liability for breach of section 131 of the Companies Act 1993; or

(c) where the Indemnified Person is an employee, liability for breach of any fiduciary duty owed to the Company or Related Company.

[436] Clauses 5 and 6 of the Deeds address notification and consultation, and compromises of claims, respectively. Mr Millar and Mr Mephan are precluded from relying on the indemnity in the case of liability incurred in their capacity as directors for a breach of s 131 of the Companies Act (cl 4(b)). I accept that exception must logically also apply to liability incurred in breach of fiduciary duties (which mirrors s 131 liability), and s 137 of the Companies Act.

[437] The plaintiffs also submit that cl 4(c) applies to preclude cover for Mr Millar, because he received salary payments and clearly treated himself as an ISL employee. It is not clear how that provision applies to Mr Millar in his capacity as a director of the plaintiff companies.

[438] Further, the plaintiffs say that neither Mr Millar nor Mr Mephan have complied with cl 5, which requires an indemnified person to notify the company when he or she becomes aware of any actual or threatened actions, proceedings, claims or demands, to which the indemnity might apply. The plaintiffs say there is no evidence from either Mr Millar or Mr Mephan that they had ever done this.

[439] In any event, s 162 of the Companies Act applies. Insurance and indemnities for directors' or employees' liabilities and costs are not to be provided except in accordance with s 162. Section 162(2) provides that any indemnity entered into in breach of the section is void.

[440] Section 162(3) provides that, if authorised by the Constitution, a company may indemnify a director or employee for costs in a proceeding, in which judgment is given in his or her favour, or in which he or she is acquitted, or which is discontinued, relating to the directors' or employees' actions or omissions. The Constitution may also expressly authorise indemnities for directors or employees in other proceedings (regardless of a successful defence). But criminal liability, breaches of s 131, and breaches of fiduciary duty are specifically excluded by s 162(4).

[441] However it is also clear from s 162(4)(a) that an indemnity may be provided only in relation to liability to third parties ("liability to any person *other than the company*...") (emphasis added).

[442] I accept that Mr Millar and Mr Mephan cannot rely on the indemnities in respect of the successful claims made against them in this proceeding.

***Estoppel***

[443] The defendants variously plead an affirmative defence that the plaintiffs are estopped from denying the existence of arrangements which permitted the defendants

to on-charge the cost of property management fees to the plaintiffs' tenants, and to recover the gain fees.

[444] The three elements required to establish equitable estoppel are:[67]

(a) A promise or assurance given by one party (by words or conduct) which gives rise to a belief or expectation by the other party.

(b) Reliance by the party that received the promise or assurance.

(c) Detriment arising from the reliance such that it would be unconscionable for the promising party to depart from the promise given.

[445] I do not think the defendants could reasonably seek to avail themselves of this defence as a shield to claims arising from their breaches of fiduciary duty and statutory duties owed to the property companies.

[446] In any event, these affirmative defences were not argued at hearing and I do not analyse them further.

***Quantum meruit***

[447] ISL also pleaded quantum meruit as an affirmative defence to the breach of contract claim against it by First NZ. That claim was pleaded in the following terms:

> To the extent that the Management Agreement terminated in 2005, as alleged by the Plaintiff but denied by the Second Defendant, services have been provided to the Plaintiff and value received by the Plaintiff such that the Plaintiff is required, on a quantum meruit basis, to pay a fair fee for such services and such fair fees are represented by the gain fees charged for which the Plaintiff has incurred liability (being only the amount of the shortfall in recovery from the Plaintiff's tenants in certain years).

[448] The essence of First NZ's response is:

(a) it does not dispute that ISL provided services to First NZ;

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[67] *Moorgate Mercantile Co Ltd v Twitchings* [1976] QB 225 at 241–242.

(b) it accepts that First NZ was entitled to be paid a "fair fee" for such services, but says that — as above — ISL received considerably more than a "fair fee"; and

(c) First NZ did not "freely accept" the services provided by ISL in the sense that such acceptance requires an opportunity for rejection.[68] It says there was never an opportunity for rejection because Mr Millar was at both ends of the bargain.

[449] In any event, the defendants did not lead any evidence as to what would be a fair fee for the services they say they rendered. Nor did the defendants' submissions address this issue.

[450] I do not consider that affirmative defence further.

**Remedies**

[451] All compensation or damages ordered below are subject to interest pursuant to s 10 of the Interest on Money Claims Act 2016.

***First NZ***

[452] First NZ is entitled to judgment in the following amounts:

(a) Against Mr Millar:

(i) $183,220

(ii) $204,328.87

(iii) $203,143.86

(iv) $830,000

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68 See *Cassels v Body Corporate No 86975* (2007) 8 NZCPR 740 (HC) at [46].

(total $1,420,692.73 plus GST)

(b) Against ISL:

(i) $183,220

(ii) $204,328.87

(iii) $203,143.86

(iv) $830,000

(total $1,420,692.73 plus GST)

(c) Against Mr Mephan: $450,000 plus GST

***Superstore***

[453] Superstore is entitled to judgment in the following amounts:

(a) Against Mr Millar:

(i) $644,945.26

(ii) $11,449.26

(total $656,394.52 plus GST)

(b) Against ISL:

(i) $644,945.26

(ii) $11,449.26

(total $656,394.52 plus GST)

***Springs Road***

[454] Springs Road is entitled to judgment in the following amounts:

(a) Against Mr Millar: $371,822.63 plus GST.

(b) Against ISL: $371,822.63 plus GST.

[455] As I have already noted, there cannot be double recovery by the plaintiffs.

[456] I expect the parties should be able to agree costs, but I indicate my view that the plaintiffs are entitled to 2B costs on their successful claims.

**Delay**

[457] I regret the delay in delivering this judgment.

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**Gwyn J**