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EDITOR'S INTRODUCTION

I am pleased to present the sixth edition of the *Waikato Law Review*. I thank the referees to whom articles were sent and the members of the editorial committee for their assistance.

The *Review* is proud to publish the Harkness Henry Lecture of the Rt Hon Sir Kenneth Keith, who is a long-established friend of the Waikato School of Law. His expertise in the field of international law is evident in his Lecture, and the theme of his Lecture is timely. It will be noted that, in the other articles in this *Review*, which reflect on topics in environmental law, tax, equity and criminal law, regard is had to overseas developments in assessing New Zealand law.

The significance of international law in domestic law was strikingly evident in the recent House of Lords decision in *R v Barile and Commissioner of Police for the Metropolis, Ex Parte Pinochet*. Here, the House of Lords heard an appeal concerning the scope of immunity of a former head of state from the criminal processes of England. In the course of his speech, Lord Nicholls declared that "international law has made plain that certain types of conduct, including torture and hostage-taking, are not acceptable conduct on the part of anyone. This applies as much to heads of state, or even more so, as it does to everyone else; the contrary conclusion would make a mockery of international law". Whatever the final fate of Senator Pinochet, the House of Lords has provided a resounding affirmation of the immediate importance of international law in human affairs.

The *Review* is also pleased to publish the presentation by Christopher Flatt, the winner of the annual student advocacy contest kindly sponsored by another Hamilton firm, McCaw Lewis Chapman. His argument on recent majority decisions of the Court of Appeal indicate the inherent uncertainty of the law at the upper levels of the court system. Here again, the legal developments in the *Ex Parte Pinochet* case are of significance: the House of Lords, by a majority of three to two, upheld an appeal from the Divisional Court of the Queen's Bench Division, which had itself quashed a provisional warrant for the arrest of Senator Pinochet. This unpredictability in the outcome of litigation is, after all, the inevitable result of the infinite variability of human attitudes and behaviour, of both litigants and judges.

Professor Peter Spiller,
Editor, *Waikato Law Review*.

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THE HARKNESS HENRY LECTURE

THE IMPACT OF INTERNATIONAL LAW ON NEW ZEALAND LAW

BY RT HON SIR KENNETH KEITH*

I. "MOVING TO THE MEASURE ..."

In 1886 Oliver Wendell Holmes spoke to a University audience of the "secret isolated joy of the thinker who knows that a hundred years after he is dead and forgotten many men who have never heard of him will be moving to the measure of his thought - the subtle rapture of a postponed power".¹ That hidden power can be for good or for ill. The road on which we imagine we are marching - the facts on which the thought was based - may have disappeared; they may not ever have existed.

I begin with two statements of thought, statements which have had major and, I will argue, seriously misleading effects on the way we understand our law in its international setting. Again I take them from about 100 years ago, but similar statements could easily have been found 50 years ago when the firm under whose auspices I am honoured to give this lecture was established, or 40 years ago when, with a son of a founder of the firm, I began my law studies. The two statements relate to the two parts of the title to this lecture.

* Judge of the Court of Appeal of New Zealand, Professor Emeritus of the Victoria University of Wellington, Associé de l'Institut de Droit International. I am very grateful to Margaret Bedggood, Dean of the School of Law, and Warren Scotter, of Harkness Henry, and their colleagues, for the invitation to give the Harkness Henry Lecture and their hospitality. I received valuable comments on a draft of this paper from Graeme Buchanan, Scott Davidson, Alex Frame, Paul Hunt, Bill Mansfield, Robert McCorquodale, Janet McLean, Geoffrey Palmer, Diana Pickard, Paul Rishworth, Peter Spiller, Lyn Stevens and John Wallace. Because the subject matter bearing on the title is huge I have had to be selective. My selection, especially in part IV of the paper, is also partly governed by other recent writing. Because many of the matters I mention continue to evolve, I have included only limited references to developments since I gave the Lecture.

¹ "The profession of the law", Conclusion of a lecture delivered to undergraduates of Harvard University, on February 17, 1886, in *Speeches by Oliver Wendell Holmes* (1900) 22, 25-26.

The first thought, about national legislative power, was stated by A V Dicey in 1885 in the first edition of *An Introduction to the Study of the Law of the Constitution*. He declared that “Parliament ... has, under the English constitution, the right to make or unmake any law whatever”.²

The second statement, about the character and scope of international law, could be taken from any one of a large number of writers. In 1880, W E Hall, a noted English international lawyer, began the first edition of his book on *International Law* in this way:

International law consists in certain rules of conduct which modern civilised states regard as being binding on them *in their relations with one another* ... (emphasis added).

A great Victorian scientist T H Huxley once famously declared that many a beautiful theory had been slain by ugly facts.³ In parts II and III of the paper, I refer to a limited selection of some of the facts and the related law, of a century ago and of the present day, to test the theories or thoughts, “beautiful” or not, of Dicey and Hall.⁴ The main part of this paper, part IV, is concerned with institutional consequences, especially for national processes and national law, of much law being made elsewhere. The final part suggests consequences for the profession and for legal education. We must slay some theories!

II. SOME LEGAL FACTS FROM 100 YEARS AGO, WITH SOME CONTEMPORARY REFERENCES

I begin with crime, a major subject of national legislation, but in various situations the subject, in addition, of international prohibition and regulation. That additional element has long constituted a recognition that national law alone was not adequate if the problem in issue was to be adequately dealt

² (10th ed, 1959) 39-40.

³ “Biogenesis and Abiogenesis” in his *Collected Essays* (1893-1894).

⁴ Alex Frame and Paul Rishworth suggest in different ways that the discussion in the text may be unfair to Dicey, especially by taking the one quoted sentence out of context. The criticism has real force, given, for instance, Dicey’s countervailing emphasis on the sovereignty of the people (recently used by the Court of Appeal in *Lange v Atkinson* [1998] 3 NZLR 424, 463) and on the rule of law, and the teaching purpose of *An Introduction*, based on University lectures. But the sentence is very quotable, is often quoted (eg by Wild CJ in *Fitzgerald v Muldoon* [1976] 2 NZLR 615, 622) and has taken on a life of its own. And that is so even if Dicey was helping his students’ understanding by stating a fiction rather than a legal rule.

with. Over 120 years ago both the New Zealand and English courts had regard to international law in deciding whether they had jurisdiction over homicides at sea where the alleged offender was on board a foreign ship.⁵ That matter has subsequently become the subject of treaty provisions codifying the generally exclusive jurisdiction of the flag state on the high seas, a principle reflecting the freedom of the high seas and also seen at work early in this century in a dispute about the extent of coverage of New Zealand industrial awards applying to trans-Tasman shipping.⁶ While individual judges, notably Lord Mansfield (although hesitantly), national legislatures and navies moved against slavery, international agreement was also essential, especially in respect of actions on the high seas, if that scourge was to be ended.⁷

It was not just the substance of the criminal law that was being formulated internationally last century (and indeed had been for much longer when piracy and war crimes are taken into account) but also the methods for the enforcement of that law. So the second half of the nineteenth century saw the rapid development of extradition law based on an extensive network of bilateral treaties. The bulk of New Zealand's extradition arrangements can indeed be traced back to that time.⁸

To move to the month of the lecture, May 1998, a new Extradition Bill has been introduced into the New Zealand Parliament, and the Group of Eight Leaders meeting at their Summit in Birmingham have focused on what they identified as three major challenges facing the world on the threshold of the twenty-first century. One was tackling drugs and transnational crime, which, they say, threaten to sap economic growth, undermine the rule of law and damage the lives of individuals in all countries of the world. They elaborated on that challenge:

Globalization has been accompanied by a dramatic increase in transnational crime. This takes many forms, including trafficking in drugs and weapons; smuggling of

⁵ *R v Dodd* (1874) 2 CA (NZ) 598 and *R v Keyn* (1876) LR 2 ExD 63.

⁶ *Re the Award of the Wellington Cooks and Stewards Union* (1906) 26 NZLR 394 (FC).

⁷ For an excellent account see Hugh Thomas, *The Slave Trade: The History of the Atlantic Slave Trade 1440-1870* (1997) especially books 5 and 6.

⁸ *New Zealand Consolidated Treaty List* part two (1997) lists extradition treaties with 52 countries. Treaties with only 15 countries were concluded this century and only 2 of those - with Fiji, after it had left the Commonwealth and the Fugitive Offenders Act 1881 no longer applied, and the United States, replacing a treaty of 1794 - were concluded in the last 50 years. See also the list in M A Soper, *The Laws of New Zealand: Extradition and Fugitive Offenders* (1993) 65-68.

human beings; the abuse of new technologies to steal, defraud and evade the law; and the laundering of the proceeds of crime.

Such crimes pose a threat not only to our own citizens and their communities, through lives blighted by drugs and societies living in fear of organized crime, but also a global threat which can undermine the democratic and economic basis of societies through the investment of illegal money by international cartels, corruption, a weakening of institutions and a loss of confidence in the rule of law.

They elaborated on what they saw as “indispensable” international cooperation relating to money laundering, assets confiscation, combating official corruption, trafficking of human beings, joint law enforcement, high-tech crime, environmental crime and the drugs problem.

Extradition law reflected a need to deal with the movement of certain people over borders. The development of the transborder movement of information by the telegraph and post similarly required international regulation and international institutions (from 1875 in the case of the telegraph and 1891 in the case of the post). The freedom to lay telegraphic cables under the oceans was quickly recognised as one of the freedoms of the sea. In addition, the cables were protected by multilateral treaty from 1884 with the States parties (including New Zealand in respect of which there was a separate accession) undertaking to enact legislation making it an offence wilfully or negligently to damage the cables, and placing strict civil liability on those who did that damage.⁹ That is still the case, with Parliament in 1996 enacting a revised Submarine Cables and Pipelines Protection Act which expressly mentions its treaty base.

Communications technology has of course developed amazingly over the last 120 years. When in 1876 New Zealand first became linked to the Imperial cable through Sydney and “the east” to London the cost of sending a 20 word message from Sydney to London was £9.9.6, the equivalent of about \$1,000 today or \$50 a word. Even 50 years ago telecommunications were expensive and limited as appears from the fact that on an average day in 1950 the total New Zealand population of 1,900,000 made only 16 overseas telephone calls. The daily figure was nearly 100,000 when it recently became commercially sensitive; and in the early part of 1998 a weekend telephone call of any length to the United Kingdom or North

⁹ Convention for the Protection of Submarine Cables, 14 March 1884, 163 CTS 391, supplemented in 1886, 168 CTS 337, and 1887, 169 CTS 375. The provisions have been carried over into the 1982 United Nations Convention on the Law of the Sea articles 113 and 114 (see also article 115) which became binding on New Zealand in 1996, 1982 ILM 1621.

America cost \$15 maximum. As well, there are the new technologies, unimagined even 50 years ago, of the fax and the internet.

In a fascinating recent paper, Terence O'Brien, the Director of the Centre for Strategic Studies, discussed as one aspect of the information technology revolution its

impact on the actual conduct and system of government, both nationally and internationally. At the national level greater accountability and transparency forced upon political leadership by information technology suggest that the revolution is reinforcing basic features of democracy. More open politics and societies are the result. International relations should grow more peaceable. The effects on authoritarian states like China have been to enlarge understanding, ideas and influence amongst populations previously restricted, even suppressed. The role of communications in the collapse of East Germany, and their contribution to the breaking down of the Berlin Wall, six years ago, is widely regarded to have been significant.¹⁰

He balanced against that impact and diminishing national control a governmental move "towards reliance upon international organisations, regimes, rules, systems and law to meet the lengthening list of transnational challenges which the revolution is bringing".

Information and ideas recorded in books had of course long been moved across borders. While national copyright legislation could protect the intellectual property of the author and publisher within national jurisdictions (and indeed throughout the Empire) it could not provide protection in foreign countries. Their cooperation, generally based on bilateral or multilateral understandings and treaties, was required if the "piracy" of which Charles Dickens for instance vigorously complained on his tours of America was to be defeated.¹¹ The first major multilateral development was the establishment of the Berne Union in 1886 with the signing of the Convention for the Protection of Literary and Artistic Works. The treaty setting up the Paris Union protecting Industrial Property (patents) had been signed three years earlier. International copyright has been in the news in

¹⁰ T O'Brien, "The Impact of Information Technology on Politics and Powers in International Affairs", paper given at the TUANZ Conference, Wellington, 17 July 1997.

¹¹ Eg Fred Kaplan, *Dickens : A Biography* (1988) 124-125, 127-128, 133. The New Zealand Copyright Act 1913 replaced 17 imperial statutes, dating from 1734 to 1888, including at least four concerned with international copyright.

recent days with the enactment by the New Zealand Parliament of the budget measure permitting parallel importing.¹²

So far I have been mainly speaking about the movement of people and things across national borders or actions in international areas, especially the high seas. But the international law makers were also giving attention to actions confined within national borders which were seen as having international consequences.¹³ By 1900 the International Association for Labour Legislation was established with the objective, among others, of furthering the study of procuring uniformity in the various labour codes. This was a step on the way to the establishment of the International Labour Organisation in 1919 and the explicit recognition, first, that “the failure of one nation to adopt humane conditions of labour is an obstacle in the way of other nations which wish to improve the same standards in their own countries” and, second, of the essential principle that labour is not simply a commodity of trade. That second principle can be seen at work - although its exact parameters continue to be a matter of controversy - in the recent decision of the seven permanent members of the Court of Appeal in *Aoraki Corporation Ltd v McGavin*.¹⁴ After calling attention to the sharp changes to employment law which Parliament had introduced by enacting the Employment Contracts Act 1991, the principal judgment continued:

Nevertheless it is important to emphasise again that the personal grievance provisions are part of the overall balance reflecting the special characteristics of employment contracts and under which ... employees and employers have mutual obligations of confidence, trust and fair dealing.¹⁵

The G8 at their Birmingham meeting have made a related statement in their renewal of support

for global progress toward the implementation of internationally recognized core labour standards, including continued collaboration between the ILO and [World Trade Organisation] secretariats in accordance with the conclusions of the Singapore [WTO Ministerial] conference and the proposal for an International Labour

¹² Copyright (Removal of Prohibition on Parallel Importing) Amendment Act 1998.

¹³ This was not a new development. The treaties of Westphalia of 350 years ago, seen by many as marking the beginning of the modern State system, included provisions protecting minorities (1 CTS 119 and 127).

¹⁴ [1998] 3 NZLR 276.

¹⁵ At 287.

Organisation declaration and implementation mechanism on these labour standards.¹⁶

Conservation of resources in international areas is much more obviously a matter that calls for international as well as national action. While the initial understanding of the freedom of the high seas, as including an unfettered freedom to take the living resources of the sea, was based on assumptions about the inexhaustibility of the supply given the available methods of fishing, by the second half of last century some species were seen as being at risk. To take one example from the time of Dicey and Hall, the American Secretary of State in 1887 instructed his representatives in France, Great Britain, Canada, Japan, Russia, Sweden and Norway to request the governments to which they were accredited to cooperate with the United States “for the better protection of the fur seal fisheries in Bering Sea”. While on the American view there was a good prospect of successful negotiation, an unnamed colony of a foreign nation (in fact Canada) proposed “to destroy this business in the indiscriminate slaughter and extermination of the animals, in the open neighbouring sea, during the period of gestation, when the common dictates of humanity ought to protect them”. The argument being made in support of that slaughter, based on freedom of the high seas, would, in the American view, take under its protection piracy and the slave trade. Following lengthy diplomatic exchanges between the United States and the United Kingdom, the matter was submitted to arbitration. The arbitrators held in favour of the freedom of the high seas but, in accordance with the arbitration agreement, proposed regulations for the protection of the seals by regulating the places, time and method of catch. The two States agreed to that proposal.¹⁷

Environmental concerns now command, rightly, much greater international and national attention with the recognition especially at Stockholm in 1972 and Rio in 1992 of major threats to the world’s environment and the corresponding need for concerted international action to respond to the threats. Those concerns continue to include the protection of maritime mammals, as recognised in the periodic meeting of the International Whaling Commission being held this month in Oman.

The final area of fact and related law I mention is the law of armed conflict, especially the law protecting the victims of warfare. By its very nature, international armed conflict cannot be governed simply by national law, and

¹⁶ As foreshadowed by the G8, the International Labour Conference in June 1998 adopted the ILO Declaration on fundamental principles and rights at work.

¹⁷ J B Moore, *A Digest of International Law* (1906) vol 1, 890-923. See also the steps taken by the Japanese and Russian Governments (*ibid*, 922-929).

the world community has formulated that law in treaty form from 1864 onwards. Rules of customary international law had of course applied to wars from much earlier. Armed conflicts, especially internal ones,¹⁸ are distressingly still a prominent feature of the world. The substantive law has been both further elaborated and shockingly breached. In part as a consequence of those breaches, greater attention is being given to the means of implementation and enforcement, for instance in the proposals to establish a permanent International Criminal Court to be considered by the diplomatic conference to be held in Rome in June. Such a court was proposed at least as early as 1874 by Gustave Moynier, one of the founders of the International Committee of the Red Cross.¹⁹

Most of the facts and the related law, national and international, that I have mentioned, existed in the 1880s and would have been known to Dicey who after all began preparing his great work on the conflict of laws in 1882. Even if he was looking narrowly at what under “the English constitution”²⁰ the Queen in Parliament could do, his statement could not have a practical reality in an increasing range of situations. That was so for two basic reasons. The first is that some matters of real importance to the United Kingdom could not then and cannot now be the subject of national law alone. While Parliament might legislate on the matter, that legislation would be ineffective without international support and action. Secondly, not only was national power inadequate to achieve its ends in many situations, but even if it were adequate it was also sometimes constrained in those endeavours by international law, whether or not the national courts would enforce that constraint. National law has never been available to excuse breaches of international law.²¹ The facts appear to destroy or at least

¹⁸ For a concrete discussion of a modern day attempt to apply the Geneva law to an internal conflict, a process which involves rulings by the national Constitutional Court, see Frits Kalshoven, “Protocol II, the CDDH and Colombia” in K Wellens (ed), *International Law : Theory and Practice - Essays in honour of Erik Suy* (1998) 597.

¹⁹ Hall, “The first proposal for a permanent international criminal court” (March 1998) 322 *Int Rev R C* 57.

²⁰ Scots lawyers have of course long taken a different view, eg Smith, “The Union of 1707 as Fundamental Law” [1957] *PL* 99, and A W Bradley and K D Ewing, *Constitutional and Administrative Law* (12th ed 1997) 79-82 and the Scottish cases and writing they mention.

²¹ *Eg Exchange of Greek and Turkish Populations Case* PCIJ Series B No 10 (1925) 20, and article 27 of the Vienna Convention on the Law of Treaties. For a recognition of the principle by a great British (Admiralty) judge, Sir William Scott, see *Le Louis* (1817) 2 *Dods* 210, 165 *ER* 1464.

heavily qualify Dicey's statement or theory when the law of the United Kingdom is seen in its wider context.

What of Hall's? The Hall definition of international law emphasises that the rules are binding on States *in their relations with one another*. While the rules discussed above were largely prepared by governments and in form at least are binding on them in their relations with one another, most also create or are the basis of rights and duties of individuals. Those rights and duties are in addition usually the subject of national law and administered by national courts and other national institutions. So, while the extradition treaties do regulate relations between the State parties, they also provide for significant individual duties (and rights) and are applied in national courts and by national Ministers and other national officials; the law of armed conflict creates rights for victims and corresponding duties for an enemy state, and imposes duties on individuals, for instance in respect of war criminality enforceable by the enemy state, the national state and even neutral states; international copyright law creates rights and duties between individuals who are generally nationals of different states as does the cable protection law; and the affected parties under that cable law may be nationals of one and the same state, as generally will be the case of workers and employers who have rights and duties under labour conventions.

In summary, the rules in question may be binding between individuals, or between individuals and states (with the individuals having rights in some cases and duties in others); many of the rules will be enforceable through national courts and institutions; and there may be no apparent international element in the facts covered by the international rule. The rules are not simply, or even principally, binding on states "in their relations with one another". Hall's restrictive definition did not and does not square with the facts. It stands in the way of a proper understanding of the reality of international law.

Greater emphasis to the present day highlights even more the dangers of moving to the measure of Dicey and Hall.

III. SOME MODERN FACTS - AND SOME OF THE MATCHING LAW

Major, even revolutionary, changes in recent years in science and technology, in population growth, in the environment, in global financial markets, in communications, in trade patterns and in ideology have led to a rash of books with titles like *The Borderless World*, *The Work of Nations*, *The Retreat of the State*, *The End of the Nation State*, *Global Dreams: Imperial Corporations and The New World Order*, *The Global*

Neighbourhood and Twilight of Sovereignty. One of the major studies, by Professor Paul Kennedy of Yale University, is entitled *Preparing for the Twenty-First Century*. He concludes the first part of his book by referring to two major changes in the power of the State:

These global changes ... call into question the usefulness of the nation-state itself. The key autonomous actor in political and international affairs for the past few centuries appears not just to be losing its control and integrity, but to be the *wrong sort* of unit to handle the newer circumstances. For some problems, it is too large to operate effectively; for others, it is too small. In consequence, there are pressures for a “relocation of authority” both upward and downward, creating structures that might respond better to today’s and tomorrow’s forces for change.²²

We should not however assume that all is new under the sun. The most recent *Human Development Report 1997* published by the United Nations Development Programme provides a valuable reminder that some of the facts have scarcely changed since the beginning of the century. For 17 industrial countries for which there are data, their exports as a share of GDP were 12.9% in 1913, not much below the 1993 level of 14.5%. Capital transfers as a share of industrial country GDP are still smaller than in the 1890s, and earlier eras of globalisation saw far greater movement of people around the world. Today immigration is more restricted.²³

More generally, many States show every sign of insisting in particular contexts, such as trade, human rights, and the environment, on the rhetoric and practice of national sovereignty. But huge changes have occurred. And ideas whose time have come can have a real force of their own. The force of ideas is reflected in a third movement of public power which has been occurring apace.

²² P Kennedy, *Preparing for the Twenty-First Century* (1993) 131. The World Bank in its *World Development Report 1997: The State in a Changing World* (1997) addresses the effectiveness of the modern State. The report defines the State’s capability as the ability to undertake and promote collective actions effectively. A Orford and T Baird provide a valuable commentary in “Making the State Safe for the Market: The World Bank’s World Development Report 1997” (1998) 22 Melb ULR 195.

²³ United Nations Development Programme, *Human Development Report* (1997) 83. For a much older reminder, see the publication in 1686 by Gerard Malynes, Merchant, of the third edition of his *Consuetudo, vel, Lex Mercatoria or the Ancient Law - Merchant* (about commodities, money, and the exchange of money - and much else especially relating to the law of the sea).

That movement is to privatise public power, very often as a consequence of technology and related private action. Some of that private power is now and has for a long time been the subject of private law arising from practice, understandings, standard terms and agreement.²⁴ The changes present major issues about the public control of that private power and the democratic character of the public international law-making process. How for instance is anticompetitive behaviour which escapes the control of any single national regulator to be tested and if necessary checked?²⁵ I largely leave those issues for others or for another occasion.

Rather, two relevant present-day facts - New Zealand foreign trade and the movement of people in and out of New Zealand - are emphasised. The value of the goods and services exported from New Zealand is about 30% of the gross domestic product. The value of imports is about the same. (Trading in the New Zealand dollar occurs at more than 50 times that rate). For a long time the great bulk of that foreign trade was within the (former) Empire - especially to the United Kingdom - and accordingly was largely governed in essence by a single body of law, especially the major commercial statutes enacted late last century in the United Kingdom and adopted throughout the Empire. But now up to 40% of New Zealand's exports are to East Asia and about 30% of imports come from there, 20% of exports and imports are with Australia, 10% of exports are to the United States and 20% of imports are from there, and only about 7% of exports and imports are with the United Kingdom. That activity is governed by extensive bodies of international law. There is the public law operating in major but not exclusive measure between States, especially the recently enhanced law of the World Trade Organisation including the General Agreement on Tariffs and Trade. Other treaty-based law regulates the carriage of goods by sea, air and land and applies to the private relationships between the traders and carriers. And the widely accepted Vienna Convention on the International Sale of Goods generally governs the sale itself, although the parties to the contract can agree to vary or even set aside the rules in the Convention. The parties might also agree to have their disputes resolved by arbitration rather than by subjecting themselves to the courts of one or other parties, a process now facilitated by the preparation by the United Nations Commission on International Trade Law of its Model Law on International Commercial Arbitration, a model adopted, with some adaptations, by the New Zealand

²⁴ See the valuable account by Professor Roy Goode, "Reflections on the Harmonization of Commercial Law" in R Cranston and R Goode (eds), *Commercial and Consumer Law: National and International Dimensions* (1993) ch 1.

²⁵ Eg *Economist* 4 July 1998, 14, 77-78.

Parliament in the Arbitration Act 1996 for local arbitrations as well as for international ones.

Similarly, the movement of people in and out of New Zealand cannot be simply the subject of New Zealand law. Their contracts of carriage will generally be governed by the Warsaw Convention on Carriage by Air of 1929 and its treaty and contractual amendments. Their travel may be facilitated by visa abolition or fee waiver agreements or by agreements (as with Australia) for free entry. In some circumstances the United Nations Convention and Protocol on the Status of Refugees will be relevant, as may provisions of the International Covenant on Civil and Political Rights, the Convention on the Rights of the Child and the Convention on Torture.²⁶ Some figures highlight the practical significance of those bodies of law. Forty years ago only 1,000 people flew into and out of New Zealand each week. The figure is now about 70,000 a week, or 4,000,000 a year, an increase by a factor of 70 (and the passenger mile figure will have increased by more). The number of refugee applications has also increased markedly, for instance from 27 to 1977 in the period 1987-1991, a matter mentioned by the Court of Appeal in suggesting the need for legislation regulating that matter.²⁷

The facts and related law considered so far have emphasised public, governmental law - especially that made by treaty internationally and legislation nationally. But to return to an earlier point, an increasingly extensive range of international activity is regulated by private law, established by the practice, custom or codes of ethics of an industry, occupational group or profession; or by the standard terms prepared for instance by the International Chamber of Commerce; or by the insurance and shipping interests; or by restatements by experts; or by a set of rules and institutions agreed to by the members of an industry. An example of the first is the Hippocratic oath and of the last the body of law governing the world diamond industry.²⁸ In some cases the private agreement will supplement the public law. In other cases it will stand essentially alone, although in the end it will be referable to some national systems of law if

²⁶ The Refugees and Torture Conventions are considered in *S v Refugee Status Appeals Authority* [1998] 2 NZLR 291; and the International Covenant on Civil and Political Rights and Children's Convention is considered in *Rajan v Minister of Immigration* [1996] 3 NZLR 543.

²⁷ *Butler v Attorney-General*, unreported, CA181/97, 13 October 1997.

²⁸ Bernstein, "Opting out of the legal system: extra legal and contractual relations in the diamond industry" (1992) 21 JLE 115.

only at the point when an exercise of the private law is being recognised, enforced or challenged.

As already hinted, not all aspects of this development are benign. Professor Harry Arthurs, of Osgoode Hall Law School, has made that point very effectively in recent papers, including one given in Wellington, called "Globalization and its Discontents".²⁹ The United Nations Secretary-General, Kofi Annan, has also underlined the worry in his proposals relating to "uncivil society" as he calls it.³⁰ But, to repeat, the major problems arising from private power which has escaped from national regulation and control are not my subject on this occasion. I am keeping closer to home.

I return to the treaties to which New Zealand is party and to related statutes. As appears from the invaluable, recently published *New Zealand Consolidated Treaty List* (2 parts 1997), New Zealand is or has been party to about 2,000 treaties and, according to a Law Commission list, almost 200 of the approximately 600 public Acts on the statute book have possible implications for New Zealand's international obligations arising from those treaties and other sources.³¹ The whole list demonstrates the pervasive effect of international law on our national law. Another Law Commission publication briefly indicates both the functions and subject matter of treaties.³² So far as functions are concerned, they can be compared to constitutions, legislation, conveyances, gifts and contracts.³³ Their wide-ranging subject matter includes war and peace, disarmament and arms control, international trade, international finance, international commercial transactions, international communications, international spaces, the environment, human rights, labour conditions and relations, and other areas of international economic, social and cultural cooperation.

I take two statutes from both the beginning and the end of the alphabetical list of New Zealand statutes to suggest the pervasiveness of international

²⁹ See also Arthur, "Globalization of the Mind: Canadian Elites and the Restructuring of Legal Fields" (1997) 12 CJLS/RCDS 219.

³⁰ *Renewing the United Nations: A Programme for Reform: Report of the Secretary-General* (14 July 1997) A/51/950 paras 143-145, 209.

³¹ Law Commission, *New Zealand Guide to International Law and its Sources* (1996 NZLC R34) Appendix C.

³² "Treaties: What are they, what do they do, how are they made, and how are they given effect?" (1991) in Legislation Advisory Committee, *Legislative Change: Guidelines on Process and Content* (rev ed 1991 Report 6) 76, 77-78.

³³ Lord McNair, "The Functions and Differing Legal Character of Treaties" (1930) 11 BYIL 100 (reprinted as Appendix A to his *Law of Treaties* (1961)).

law in our national law and to illustrate some particular characteristics of the law in issue and the international processes involved. Those statutes are the Abolition of the Death Penalty Act 1989, the Accident Rehabilitation and Compensation Insurance Act 1991, the Weights and Measures Act 1987 and the Western Samoa Act 1961.

The first enabled New Zealand to be the first State to accept the additional protocol to the International Covenant on Civil and Political Rights (ICCPR) prohibiting the death penalty - an action which the government took without giving Parliament or the public any chance to comment. That human rights instrument, like the two Covenants, has no express provision for withdrawal. There are good arguments, now accepted by the Human Rights Committee, the United Nations Secretariat and the Australian Attorney-General, that there is also no implied unilateral power of withdrawal.³⁴ That prohibition on State action is to be related to the essential character of human rights and fundamental freedoms, especially as that character has been perceived since 1945.

The accident rehabilitation and compensation statute is designed, among other things, to give effect to New Zealand's obligations under International Labour Conventions which it has ratified. Those Conventions are subject to long-established international complaints procedures. Those procedures have been used in recent years, first to make it clear that New Zealand has been in breach in certain respects of its obligations, and second to cause steps to be taken to ensure compliance. The Conventions are to be related back to the proposition mentioned earlier and established early in the century that setting up and maintaining humane labour conditions in a nation may require international agreement as well as national action. International trade was now seen as requiring agreed minimum labour standards.

The Weights and Measures Act incorporates into New Zealand law the basic measurements in accordance with the Convention of the Metre 1875, to which New Zealand acceded as recently as 1991. In a practical sense a country which engages in international trade, especially to the extent that New Zealand does, could not conceivably stand aside from that international system. The parties to the Convention agreed to establish and maintain a permanent international scientific bureau of weights and measures, in Paris. The bureau is charged with several responsibilities including all

³⁴ The Secretariat and Committee took that position in 1997 when the Democratic People's Republic of Korea purported to withdraw from the ICCPR, while the Australian Attorney-General had expressed it in 1994 ([1995] AYIL 470, quoting Senate Debates (28 November 1994) 3372).

comparisons and verifications of the new prototypes of the metre and kilogram. The Convention also provides for the ongoing administration and supervision of the work of the bureau.

The Western Samoa Act marked the end of New Zealand's responsibility for that country, and was enacted in accordance with the decision of the United Nations based on a referendum of the Samoan people that Samoa was to become independent. That responsibility had always been governed by international law, first when Western Samoa was occupied enemy territory from 1914 to 1919, second as a mandated territory from 1919 to 1946, and third as a trust territory from 1946 to 1961.³⁵ As with the ILO, there were reporting and monitoring processes, under the Permanent Mandates Commission of the League of Nations and the Trusteeship Council of the United Nations.

IV. LAW MADE ELSEWHERE - SOME INSTITUTIONAL ASPECTS

The developments, both ancient and modern, that I have sketched raise a series of important questions about how these extensive bodies of law are (1) developed, (2) accepted and implemented by (3) Parliament, (4) courts and (5) internationally, especially so far as New Zealand is concerned. In this part of the paper I emphasise treaties, but the other sources of international law should not be neglected. The relative brevity of the discussion in sections (2) and (3) below and to some extent in (4) reflects extensive recent writing in those areas.

1. The preparation of the treaty

The first stage is agenda setting and then the negotiation and preparation of the text of the proposed instrument. The orthodox position under the New Zealand constitution is that the negotiation of treaties is an executive function as part of the royal prerogative. It is exercised in practice by the Minister of Foreign Affairs and Trade and other ministers and their officials, including ambassadors and representatives at international organisations.

³⁵ For the three stages see eg *In Re Gaudin* (1915) 34 NZLR 401, 406-407; the mandate, the Samoa Act 1921, A Frame, *Salmond: Southern Jurist* (1995) 189-198, and the text at nn 54 and 81-86; and the trusteeship agreement, the 1946 Amendment Act and Boyd and Aikman in Angus Ross (ed) *New Zealand's Record in the Pacific Islands in the Twentieth Century* (1969) 189-270 and 308-341.

The prerogative and the practice are consistent with the rules of international law about treaty making.³⁶

It does not follow of course that the government cannot involve others in these processes, by giving notice and relevant information, by seeking information, by consultations and by having others directly involved in the international negotiation, for instance as members of the delegation. That wider involvement is actually required by the Constitution of the International Labour Organisation: union and employer representatives participate in its processes, including the drafting of conventions, equally with government representatives. The World Conservation Conference of the International Union for the Conservation of Nature and the International Red Cross and Red Crescent Conferences also provide instances of governmental and non-governmental representatives meeting together. A notable recent development in United Nations diplomacy is the calling of non-governmental organisation conferences in parallel to the major conferences held for instance on human rights, women, and the environment and development.³⁷

New Zealand practice over a lengthy period also provides instances of wide interest group involvement. The Secretary of Foreign Affairs and Trade has for instance provided an interesting account of the processes of consultation followed in the Uruguay Round negotiations which led to the setting up of the WTO and the extensive related agreements.³⁸ Such requirements and practices recognise the realities that much law is being made elsewhere and that once the text is settled it is much more difficult for relevant non-governmental interests to be accommodated. It is to be hoped that the government will respond positively to the first related recommendation made by the Law Commission in its 1997 report on *The Treaty Making Process* that

³⁶ Eg Lord Atkin in *Attorney-General for Canada v Attorney-General for Ontario* [1937] AC 326, 347-348, and article 7(2) of the Vienna Convention on the Law of Treaties. For recent United Nations publications relating to the multilateral processes of law making see United Nations, *International Law on the Eve of the Twenty-First Century: Views from the International Law Commission* (1997) and *Making Better International Law: the International Law Commission at 50* (1998).

³⁷ Eg Chinkin, "Global Summits: Democratising International Law-making?" (1996) 7 PLR 208.

³⁸ Nottage, "The GATT Uruguay Round 1984-1994: 10 years of consultation and cooperation" (August 1994) 3(3) MFAT Record 17.

the value of notification to and consultation with Parliament and affected or interested groups at the negotiating stage be recognised, with the purpose of developing and formalising such practices.³⁹

Indications of a positive response appear from the form of the National Interest Analysis relating to certain treaties (mentioned under the next heading) which will require the government to report to Parliament on the consultations it has undertaken in respect of those treaties which are now to be tabled.

2. The acceptance of the treaty

The acceptance of the text, once its negotiation is completed, as binding on New Zealand is also part of the prerogative power of the executive and that too is consistent with international law requirements.⁴⁰ But again practice in New Zealand and elsewhere shows that wider public and, in particular, Parliamentary involvement is possible and indeed required by democratic principle. In fact the government has just accepted significant parts of the recommendations of a Parliamentary select committee, recommendations which were similar to the second recommendation made by the Law Commission in its *Treaty Making* report, enabling Parliament and the public to scrutinise the government's proposed actions in respect of treaties which are subject to a distinct stage of ratification, accession or acceptance.⁴¹ The process is to be facilitated by the preparation of a National Interest Analysis setting out the domestic implications of the treaty and the reasons New Zealand should accept the treaty and, as noted, the consultations undertaken

³⁹ Law Commission, *The Treaty Making Process: Reform and the Role of Parliament* (1997 NZLC R45) para 144.

⁴⁰ See the judgment of the Privy Council and the provision of the Vienna Convention mentioned in n 36 above.

⁴¹ See the Report of the Foreign Affairs, Defence and Trade Committee, *Inquiry into Parliament's Role in the International Treaty Process* 1997 AJHR 1.4A 8-9, Law Commission report n 37 above paras 162-186, the Government response to the Committee Report 1998 AJHR A5 (indicated as well in the speech of the Minister of Foreign Affairs & Trade launching the *Consolidated New Zealand Treaty List* given on 17 December 1997), the related debate and decisions of the House of Representatives, 28 May 1998, Hansard 9419-9443, and a Cabinet Office Circular of 6 July 1998. The Law Commission report refers to discussions of New Zealand and other practice. See also Gobbi "Enhancing Public Participation in the Treaty Making Process: An Assessment of New Zealand's Constitutional Response" (1998) 6 *Tulane J of Int and Comp L* 57, and papers given to the Conference on Treaties and New Zealand Law, Wellington, 7 and 8 August 1998, International Law Association (New Zealand Branch).

or proposed. This step rightly recognises that the importance of the treaty making process does require greater Parliamentary and public participation than has recently occurred.⁴² Practice, in Australia⁴³ as well as in New Zealand, will indicate whether that participation should take a more extensive form.

3. *The drafting of implementing legislation*

The third Law Commission recommendation relates to the legislative implementation of treaties:

so far as practicable, legislation implementing treaties or other international instruments [should] give direct effect to the texts, that is, use the original wording of the treaties, and that when that is not possible, the legislation [should] indicate in some convenient way its treaty or other international origins.⁴⁴

While there has not been a formal response to that recommendation there are encouraging signs that those responsible for the preparation of legislation appear to have accepted the value of not providing a legislative gloss to treaty language when it is designed for direct application. The Adoption (Intercountry) Act 1997 which simply provides that the Convention has the force of law in New Zealand is to be contrasted with the Guardianship Amendment Act 1991. This Act was intended to implement the Abduction Convention, but created unnecessary difficulty by using wording different from that in the Convention, a difference which encouraged arguments that Parliament was intending a different result.⁴⁵

⁴² For a notification of the first batch of treaties due to come before Parliament under the new procedure see 501 *LawTalk* 18; and for an account of earlier New Zealand practice, see (1964) 1 NZULR 272.

⁴³ A major recent step was the report of the Senate Legal and Constitutional References Committee, *Trick or Treaty? Commonwealth Power to Make and Implement Treaties* (November 1995). The Australian Government responded positively to that Report which proposed the tabling of all treaties (see Law Commission report No 45 84-93). Part of the outcome is to be seen in the stream of reports of the Joint Standing Committee on Treaties of the Parliament of the Commonwealth of Australia. By June 1998 sixteen have been published, the latest on the OECD Convention on Combating Bribery. See Burmester at the ILA Conference in n 41 above.

⁴⁴ Report n 39 above, para 195.

⁴⁵ For an earlier discussion of those problems see "International Business Law" *New Zealand Law Conference April 9-13 1996 Conference Papers Volume I*. See also n 89 below about inaccurate legislative implementation of an arbitration treaty.

Not all treaty provisions are written in a way which allows direct application of their terms by the courts. Indeed, many expressly contemplate that national legislation will be enacted integrating the substance of the treaty into national law, for instance by creating new offences and imposing penalties or establishing new rights and duties for individuals. That legislation might use the wording of the treaty to a greater or lesser extent or it might bear no particular relationship to it. As the third Law Commission recommendation indicates, it might refer - or not - to the treaty. There is real value in including a reference, for those administering the legislation, interpreting it or considering its amendment or repeal.⁴⁶

In other cases, the judgment may be made by those responsible that no legislation is required to give effect to the treaty - for instance because it operates only between States and does not affect the rights and duties of individuals (as with major parts of the Charter of the United Nations); or because it confirms or declares customary international law which is part of New Zealand law (as with parts of the Vienna Convention on the Law of Treaties); or because New Zealand law already complies with it (or is thought to) (as with the Convention on the Rights of the Child, subject to the reservations which were made). Problems can of course arise if that judgment turns out to be faulty.

Other legislation may be enacted with no reference at all to international obligations which, it might later be contended, are relevant to its operation. As indicated in the next part of this paper, that omission does not necessarily exclude those obligations being invoked as relevant to the interpretation or operation of the legislation.⁴⁷

⁴⁶ For instances of the apparently consequential neglect of relevant treaties see *R v Dechamsakun* [1993] 1 NZLR 141, a slavery case which draws on dictionary definitions but not on the binding treaty definitions provided by the 1926 and 1956 Slavery Conventions, 60 LNTS 253 and 266 UNTS 40; and the Medicine Amendment Act 1989 repealed by the Medicine Amendment Act 1990.

⁴⁷ The choice of legislative form has been the subject of recent extensive discussion, see eg the 1996 and 1997 Law Commission reports nn 29 and 37 above and the sources they refer to including those listed in n 6 of Report 34. An essential step is to ensure that those responsible for the preparation of legislation take relevant treaty and other international obligations into account. The *Cabinet Office Manual* (1996) 5-26 and 122, 124, requires Ministers when proposing legislation to report on compliance with relevant international obligations; see also n 70 below.

4. *International law in the courts*

Last year the Court of Appeal ruled that the police could have access by way of a search warrant to the cockpit voice recorder (the black box) recovered from the Ansett Dash 8 which crashed near Palmerston North and held by the Transport Accident Investigating Commission. It also held that the Commission could append extracts from the transcript of the record to its accident report. The Court rejected the arguments made by the Air Line Pilots' Association that the search warrant and reporting powers were constrained in some way by an annex to the Chicago Convention on International Civil Aviation 1944, titled "Aircraft Accident and Incident Investigation".⁴⁸

In answering the question whether the Chicago Convention was part of the law of New Zealand, the Court said that it was

well established that while the making of a treaty is an Executive act, the performance of its obligations, if they entail alteration of the existing domestic law, requires legislative action. The stipulations of a treaty duly ratified by the Executive do not, by virtue of the treaty alone, have the force of law.⁴⁹

The Court accordingly turned to the relevant legislation, consisting of five Acts and three sets of subordinate instruments, to see whether the necessary legislative action had been taken. It concluded that "some of the provisions of the convention and annexes are appropriate in their subject matter and drafting for direct application in the law of New Zealand, others require detailed national legislation, while still others do not require national legislation at all".⁵⁰ The Court distinguished between the different roles the aviation convention played and the different ways in which it may be implemented by the parties to it and in which it may operate in national law. I use some of the categories suggested by the Court and also by the Law Commission.⁵¹ It will be seen that some are better established than others and that it can be difficult to draw lines between them.⁵²

⁴⁸ *New Zealand Air Line Pilots' Association v Attorney-General* [1997] 3 NZLR 269.

⁴⁹ At 280-281, citing Lord Atkin speaking for the Privy Council in *Attorney-General for Canada v Attorney-General for Ontario* [1937] AC 326, 347.

⁵⁰ At 285.

⁵¹ See the reports in nn 31 and 39 above.

⁵² Because of the emphasis in much writing on international human rights (in part related to the 50th anniversary commemoration of the Universal Declaration of Human Rights) and because I have recently twice considered the place of international human rights in New Zealand Courts, I give less attention to cases in that area. See "The application of

(a) *A constitutional role*

The Chicago Convention recognises that States have sovereignty over the airspace above their territory and territorial sea. Those provisions, which, according to the Court, “incorporate principles of customary international law, are reflected in fundamental constitutional arrangements and leave the States parties free to exercise their authority recognised by international law”.⁵³ A few years earlier in an immigration case the Court drew attention to the statement by a Commonwealth Judicial Colloquium of the vital duty of the judiciary to interpret and apply national constitutions, ordinary legislation and the common law in light of the universality of human rights.⁵⁴ Kirby J in a recent judgment in the High Court of Australia used an interpretative principle that on a constitutional question which was finely balanced it was appropriate for the judges to favour an interpretation of the Constitution conforming with principles of universal and fundamental rights rather than an interpretation involving a departure from the rights.⁵⁵ Earlier in this century New Zealand and Australian judges similarly looked to international law in finding the sources and limits of the powers of their Parliaments to deal with the government of the mandated territories of Western Samoa and New Guinea.⁵⁶ Later in this paper I quote from a 1990 judgment of the House of Lords which in a very understated way recognised the supremacy of European Community law over the law of the United Kingdom. As *The Times* editorialised at the time, A V Dicey would not have been amused.

international human rights law in New Zealand” in “Developing Human Rights Jurisprudence” (1998) 7 *Seventh Judicial Colloquium on the Domestic Application of Human Rights Norms at Georgetown, Guyana, 1996* 47, also published in (1997) 32 *Texas Int LJ* 401; and “Roles of the Courts in New Zealand in giving effect to international human rights - with some history” (one of a series on the 50th Anniversary of the UDHR) (1999) 29 *VUWLR* 27.

⁵³ *New Zealand Air Line Pilots' Association v Attorney-General* [1997] 3 NZLR 269, 284-285. Consider also the majority decision in *R v Keyn*, n 5 above, which can be read as recognising the freedom of States under international law to claim territorial seas and *facilitating* but not requiring the making of jurisdictional claims.

⁵⁴ *Tavita v Minister of Immigration* [1994] 2 NZLR 257, 266. For the latest statement from the Judicial Colloquium, see “The Georgetown Conclusions on the effective promotion of human rights through law” [1996] PL 562.

⁵⁵ *Newcrest Mining (WA) Ltd v The Commonwealth* (1997) 147 ALR 42, 147; see similarly *Kartinyeri v Commonwealth* [1998] HCA 22 paras 166-167; 152 ALR 540, 598-600.

⁵⁶ See further part II(1) of the human rights paper, n 52 above, the *Award* case n 6 above, and the Samoan citizenship cases discussed later in this paper.

(b) *Customary international law as part of the law of New Zealand*

Courts in New Zealand appear to have proceeded on the assumption, as William Blackstone put it over 200 years ago, that customary international law (or in his terms the law of nations) is part of the law of the land.⁵⁷ Some treaties may be evidence of customary international law or declaratory of it. One recurring instance is the use by courts of the provisions of the Vienna Convention on the Law of Treaties relating to good faith compliance with treaties and their interpretation.⁵⁸ Treaties and proposals for treaties have also been among the material drawn on in decisions about foreign state immunity, a matter which is not the subject of legislation in New Zealand unlike the position in a number of other common law countries. Those decisions all proceed on the basis that that part of customary international law may deny New Zealand courts the jurisdiction which they would normally be able to exercise. The immunity rules might also be used in the interpretation of legislation apparently conferring jurisdiction on a court.⁵⁹

(c) *Treaties as relevant to the determination of the common law*

Defamation cases in the United Kingdom and New Zealand have drawn on provisions of the European Convention on Human Rights and the International Covenant on Civil and Political Rights and their elaborations by the relevant treaty bodies in determining the balance between freedom of expression and the protection of reputation. (The cases also illustrate the point made earlier about the headings I am using, since they could be included under the preceding heading.) The recent Court of Appeal judgment on defamation in the *Lange* case⁶⁰ refers, for instance, to the European Convention and the ICCPR as well as to a wide range of legislation (not all directly concerned with political speech), writers from Coke and Milton in the seventeenth century, Mill, Stephen and Dicey in the nineteenth century to Hogg in this, judgments from seven jurisdictions and law reform proposals. Decisions of the European Court of Human Rights relating to political defamation and interpreting European Convention wording which is similar to that of the Covenant are given some emphasis. That Court has stressed that freedom of speech constitutes one of the

⁵⁷ *Commentaries*, book IV, ch5.

⁵⁸ *Eg New Zealand Air Line Pilots' Association v Attorney-General* [1997] 3 NZLR 269, 289.

⁵⁹ *Marine Steel Ltd v Government of the Marshall Islands* [1981] 2 NZLR 1, *Buckingham v Hughes Helicopter* [1982] 2 NZLR 739, *Reef Shipping Co Ltd v The Ship "Fua Kavenga"* [1987] 1 NZLR 550, *Governor of Pitcairn v Sutton* [1995] 1 NZLR 426 (especially 433-434), and *Controller and Auditor-General v Davison* [1996] 2 NZLR 278 (especially 305, 306-307).

⁶⁰ *Lange v Atkinson* [1998] 3 NZLR 424.

essential foundations of a democratic society and one of the basic conditions for its progress and for each individual's self-fulfilment. With much if not all of that material cited, the treaties and the judicial explication of them might be seen not so much as a formal source of New Zealand law as a material or literary source on which courts properly draw.⁶¹ The use made by the Court of Appeal in a recent criminal legal aid case⁶² of determinations of the Human Rights Committee can be considered in the same way.

(d) The interpretation of legislation by reference to international law and treaties

Over a long period the courts have stated the presumption or principle of statutory interpretation that, so far as its wording allows, legislation should be read in a way which is consistent with New Zealand's international obligations. An example is the black box case⁶³ which included references to cases about immigration, child abduction, foreign state immunity, the Treaty of Waitangi and income tax. Sometimes the approach may be expressly related to ambiguity in the legislation, as in a case about dumping duty,⁶⁴ but ambiguity does not appear as a necessary prerequisite in the run of judgments.

Much will turn on the drafting of the legislation and of the treaty. I consider in turn the varying legislative forms, mentioned earlier. If the treaty text is directly part of the law (as may happen with no official New Zealand action at all) the courts have stressed the importance of using international methods of interpretation. They have used a valuable statement made by Lord Wilberforce (following Lord Wright) that they should determine the meaning unconstrained by technical rules of English law, or of English precedent, but on broad principles of general acceptance.⁶⁵ They have also

⁶¹ See eg the valuable discussion by Clive Parry, *The Sources and Evidences of International Law* (1965) ch 1, drawing on Salmond and related writing.

⁶² *Nicholls v Registrar Court of Appeal* [1998] 2 NZLR 385.

⁶³ *New Zealand Air Line Pilots' Association v Attorney-General* [1997] 3 NZLR 269, 289. In the maritime *Award* case, n 6 above at 428, two of the Judges quoted a passage in almost identical terms from the judgment of a great international lawyer, Sir Robert Phillimore, in *R v Keyn*, n 5 above, at 85.

⁶⁴ *Auckland Harbour Board v Controller of Customs* [1992] 2 NZLR 392, 396.

⁶⁵ *James Buchanan & Co Ltd v Babco Shipping and Forwarding (UK) Ltd* [1978] AC 141, 152, eg in *King-Ansell v Police* [1979] 2 NZLR 531, 537, 540; *New Zealand Maori Council v Attorney-General* [1987] 1 NZLR 641, 714; *Baltic Shipping Co Ltd v Pegasus Lines SA* [1996] 3 NZLR 641, 647; see also *CBI NZ Ltd v Badger Chiyoda* [1989] 2 NZLR 669, 682.

referred to the provisions about the interpretation of treaties codified or declared in the Vienna Convention on the Law of Treaties.⁶⁶ The general rule which that Convention states has been compared to the direction stated in s5(j) of the Acts Interpretation Act 1924:

A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.⁶⁷

That direction can be in conflict or at least in a tension with principles and values of the wider legal and constitutional system arising beyond the particular measure. One matter bearing on that is the interpreter's assessment of the scope and significance of the context and the related principles and values, and the relative weight to be given to it.⁶⁸

The particular text - treaty or statute - may itself emphasise the international element. The United Nations Convention on Contracts for the International Sale of Goods (which has been part of the law of New Zealand since 1995) provides:

Article 7

(1) In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

(2) Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

The Arbitration Act 1996 contains in section 3 guidance on the material that can be used in interpreting the Act which is closely based on the Model Law on Arbitration prepared by the United Nations Commission on International Trade Law:

⁶⁶ *New Zealand Maori Council v Attorney-General* [1987] 1 NZLR 641, 682, and *New Zealand Air Line Pilots' Association v Attorney-General* [1997] 3 NZLR 269, 289.

⁶⁷ Article 31(1); see other provisions of articles 31, 32 and 33 relating to context, drafting history, practical application and multilingual texts; and also cl 5(1) of the Interpretation Bill currently before Parliament, a provision which draws (although in its current Parliamentary form incompletely) on the Vienna wording, see Law Commission, *A New Interpretation Act* (1990 NZLC R 17) ch III and appendix D.

⁶⁸ See paras 44-49, 54-58, 72 and 261 of the Law Commission report, "International Law and New Zealand Municipal Law" in J F Northey (ed) *The A G Davis Essays in Law* (1965) 130, 132-133, and the discussion of the *Lesa* case, n 83 below.

The material to which an arbitral tribunal or a court may refer in interpreting this Act includes the documents relating to the Model Law ... and originating from the United Nations Commission on International Trade Law, or its working group for the preparation of the Model Law.

To help that process the Law Commission reproduced two of the major documents relating to the Model Law in its report on *Arbitration*.⁶⁹

Instead of incorporating the relevant treaty text, the legislature may attempt to give effect to it by conferring or controlling powers to make regulations, rules and decisions in terms of “international agreements”, “international obligations” and “conventions”. At least 40 such statutory provisions are to be found in the statute book. They cover a wide range of activity including border control; transport by air, land and sea; natural resources including fisheries; Antarctica; animal health; intellectual property; privacy; diplomatic privileges and immunities; international trade including tariffs and the operations of the producer boards; taxation; and recognition of foreign qualifications. Because of their very terms a court may have to determine what the relevant texts are, the powers they confer and the limits they impose. The action taken under the statute may then be tested against that text.

The particular legislation may present a further issue since some statutes provide only that the relevant authority is to “have regard to” or “take into account” the obligation, as opposed to a direction that it must “give effect” to, or “act consistently” or “not act inconsistently”, or “observe” the international rules. The latter, stricter set of obligations adopts the proper approach. An authority required only to “have regard to” the international obligation might consider itself free to breach the obligation (once it had had regard to it), with consequent problems for New Zealand’s compliance with its international obligations.⁷⁰

The drafting of the relevant provision of the Tokelau Act 1948 (section 3B enacted in 1996) highlights another issue about the drafting and interpreting

⁶⁹ Law Commission, *Arbitration* (1991 NZLC R20) 279-351. See paras 205-208 for the reasons for including s 3.

⁷⁰ Compare the wording of the successive ss 4(2) of the 1990 and 1996 Ozone Layer Protection Acts. The later provision correctly requires consistency with rather than (mere) regard to the relevant international obligations. Changes in the same sense were made to the Fisheries Bill 1995 in the course of its passage through Parliament, see the chapter on International Obligations in *Report of the Legislation Advisory Committee 1 January 1994 to 31 December 1995 Recurring Issues* (Report No 9 June 1996), especially paras 75-82.

of such provisions which was recently considered by the High Court of Australia in a case relating to the rights of New Zealand television producers under the Closer Economic Relations Agreement.⁷¹ Since 1996, the Fono of Tokelau has had powers to make rules for the peace, order and good government of Tokelau, but any rule that is inconsistent with any international obligation of, or applying in respect of, Tokelau “shall, to the extent of the inconsistency, be of no effect”.⁷² That explicit consequence is not drawn in any of the other statutory provisions referred to in the preceding paragraph. Nor was it drawn in the relevant provision of the Australian Broadcasting Services Act in the *CER* case. Section 160 requires the Australian Broadcasting Authority to “perform its functions in a manner consistent [among other things] with Australia’s obligations under any convention to which Australia is a party or any agreement between Australia and a foreign country”. All judges agreed that the Authority had not performed its functions in a manner consistent with the *CER* agreement. Sir Gerard Brennan in one of his final judgments as Chief Justice would have held the non conforming provisions of a challenged standard to be invalid and of no effect.⁷³ But the other four judges held that while an act done in breach of section 160 was unlawful it was not invalid.⁷⁴ Their reasons included the following:

- not every obligation under section 160 has a rule-like quality which can be easily identified and applied;
- while some international obligations are relatively clear many international conventions and agreements are expressed in indeterminate language as a result of the compromises made; often their provisions are more aptly described as goals to be achieved rather than rules to be obeyed; the fact that Australia is party to 900 treaties was mentioned;
- if public inconvenience was a result of the invalidity of the act, courts have always accepted that that would be an unlikely purpose;
- the provision was to be seen as directory only, with the possible consequences of punishment being imposed⁷⁵ and declarations and injunctions being sought, but without the consequence of immediate nullity.

The approach, especially in terms of the first and second points, might be seen as giving inadequate effect to those treaty provisions which *do* have “a rule-like quality” or are “relatively clear”. In this context, as in others, the

⁷¹ *Project Blue Sky v Australian Broadcasting Authority* [1998] HCA 28 (28 April 1998); 153 ALR 490.

⁷² Tokelau Act 1948 s 3B(1).

⁷³ Paras 32-43; 501-504.

⁷⁴ Paras 94-100; 517-518.

⁷⁵ *Simpson v Attorney-General* [1955] NZLR 271, 281 being cited in support.

distinction between “self-executing” and “non self-executing” treaties found in several jurisdictions, notably the United States, may be seen as helpful. That is suggested by the comment in the black box case that the international text contemplated that national law or action would set up a process for decision, with competing considerations stated or implied within it.⁷⁶

A third legislative technique is to incorporate in the statute the substance of the treaty - or some of it. In some cases the treaty origin will be made explicit. A notable instance is provided by the New Zealand Bill of Rights Act 1990, which has been the subject of extensive judicial interpretation and commentary, in part by reference to the ICCPR, New Zealand’s commitment to which, according to its title, is affirmed by the Bill.⁷⁷

In such cases the presumption of interpretation in conformity with the international obligations is often invoked. That is to be seen, for instance, in cases in the last 20 years relating to tariffs and anti-dumping, race hatred legislation, citizenship and statelessness, the settlement of international investment disputes, international arbitration, taxation, mental health, extradition, child abduction and shipping.⁷⁸ The international text might not even be binding.⁷⁹

In other cases the statute in issue has no obvious connection to the treaty invoked. It may for instance have been enacted before the treaty was drafted and accepted, or the two texts may, at first sight at least, appear to operate in

⁷⁶ *New Zealand Air Line Pilots’ Association v Attorney-General* [1997] 3 NZLR 269, 290.

⁷⁷ Eg G Huscroft and P Rishworth (ed), *Rights and Freedoms* (1995) especially chs 2 and 3, B Robertson (ed), *Adams on Criminal Law* (loose leaf) ch 10, P Joseph, *Constitutional Administrative Law in New Zealand* (1993) ch 26, and regular contributions to the *New Zealand Law Review* by Brookfield, Rishworth, Joseph and others as well as many other articles on particular cases, eg nn 80 and 82 below.

⁷⁸ Eg *Sigma Agencies Ltd v Collector of Customs (Northern Region)* [1997] 1 NZLR 647; *Customs Agents Wellington Ltd v Comptroller of Customs* [1994] 2 NZLR 759; *King-Ansell v Police* [1979] 2 NZLR 531; *Yan v Minister of Internal Affairs* [1997] 3 NZLR 450; *Attorney-General v Mobil Oil NZ Ltd* [1989] 2 NZLR 649; *Baltiman Aps Ltd v Nalder & Biddle Ltd* [1994] 3 NZLR 129; *Commissioner of Inland Revenue v United Dominions Trust Ltd* [1973] 2 NZLR 555; *Re S* [1992] 1 NZLR 363; *Mewes v Attorney-General* [1979] 1 NZLR 648; *Gross v Boda* [1995] 1 NZLR 649; and *Baltic Shipping Co Ltd v Pegasus Lines SA* [1996] 3 NZLR 641.

⁷⁹ Eg *Birds Galore Ltd v Attorney-General* (1988) [1989] LRC (Const) 928, 938-940; 90 ILR 567, 578-579, referring to *Van Gorkom v Attorney-General* [1977] 1 NZLR 535, discussed in the Georgetown paper, n 52 above, at 52.

distinct spheres. That can be seen for instance in a number of cases, some controversial, relating to immigration (and racial discrimination and rights of children and families),⁸⁰ legal aid in respect of criminal appeals and complaints to the Human Rights Committee (and the International Covenant on Civil and Political Rights)⁸¹ and the right to marry (and discrimination).⁸²

A close study of the judgments mentioned in the last two paragraphs and related cases would identify differences depending, among other things, on the drafting of the international text (and its varying force and effect) and of the legislation, any differences between the texts, differing judicial attitudes and the wider social and political context in which the issue arises. I take one controversial case to suggest the varying relevance of those matters. In *Lesa v Attorney-General*,⁸³ the Privy Council, reversing the New Zealand Court of Appeal and overruling an earlier decision of that Court,⁸⁴ held that persons born in Western Samoa between the enactment of the British Nationality and Status of Aliens (in New Zealand) Act 1928, and its repeal and replacement by the British Nationality and New Zealand Citizenship Act 1948, were natural-born British subjects in terms of New Zealand law and became New Zealand citizens under the 1948 Act when that status was first established. For the great bulk of that time Western Samoa was a mandated territory under article 22 of the Covenant of the League of Nations. In terms of that provision it had “ceased to be under the sovereignty” of Germany, and in application of “the principle that the well-being and development of such peoples form a sacred trust of civilisation” it was to be under the “tutelage” of New Zealand as Mandatory. That tutelage was subject to scrutiny by the League. Western Samoa moved to trusteeship status under the United Nations in 1946 and became independent in 1962.

After setting out the procedural history of the case and a related case, Lord Diplock mentioned that a formidable argument based on the terms of the

⁸⁰ *Ashby v Minister of Immigration* [1981] 1 NZLR 222, *Tavita v Minister of Immigration* [1994] 2 NZLR 257, *Puli'uvea v Removal Review Authority* (1996) 14 FRNZ 322, and *Rajan v Minister of Immigration* [1996] 3 NZLR 543, discussed eg by Joseph [1998] NZ Law Rev 109-116.

⁸¹ *Wellington District Legal Services Committee v Tangiora* [1998] 1 NZLR 129 and *Nicholls v Registrar of the Court of Appeal* [1998] 2 NZLR 385.

⁸² *Quilter v Attorney-General* [1998] 1 NZLR 523, criticised eg by Butler [1998] NZLJ 229.

⁸³ [1982] 1 NZLR 165 CA and JC, [1983] 2 AC 20.

⁸⁴ *Levave v Immigration Department* [1979] 2 NZLR 74 CA, relating to an Act of 1923 replaced by the 1928 Act in issue in the *Lesa* case.

1928 Act had unfortunately not been brought to the attention of the Court of Appeal and had emerged for the first time in the closing stages of the opening address of plaintiff's counsel. Lord Diplock noted that "Their Lordships will accordingly go straight to the Act of 1928 and first consider its construction independently of the Act of 1923 which it repealed". That focus on the particular wording, and in particular on the proposition that the Act was to apply to Western Samoa in the same manner in all respects as if it were part of New Zealand led the Privy Council inexorably to the conclusion that in the present context Western Samoa was part of His Majesty's dominions and within His allegiance and that birth there conferred natural-born British subject status. It was only in the last substantive paragraph of the judgment that the Privy Council moved away from the legislation and referred to the "strongest argument" to the contrary - certain resolutions about nationality in mandated territories adopted by the Council of the League of Nations shortly before the enactment of the 1923 Act. Those resolutions (which the Privy Council did not set out) provided:

- (i) that the status of native inhabitants is distinct from that of nationals of the Mandatory power;
- (ii) that native inhabitants are not invested with the nationality of the Mandatory Power by means of the protection extended to them;
- (iii) that it was not inconsistent with (i) and (ii) that individual inhabitants should voluntarily obtain naturalisation from the Mandatory Power under its own law; and
- (iv) that it was desirable that native inhabitants who received the protection of the Mandatory Power should be designated by a descriptive title specifying their status under the Mandate.

Consistently with those resolutions and in accordance with Imperial legislation agreed to at Imperial Conferences the 1923 and 1928 Acts provided for voluntary naturalisation ((iii) above). The dispute was whether the Acts had any wider effect.

The Privy Council agreed with the Court of Appeal that, although the resolutions did not impose obligations binding on New Zealand under international law (although (i) and (ii) could be seen as authoritatively declaring the position under the Covenant and Mandates and interpreting existing obligations), they would be relevant in resolving any ambiguity in the meaning of the legislation. But the Privy Council was unable, for the reasons it had already stated, to find any ambiguity or lack of clarity in that language.

The New Zealand Court by contrast had thought that the legislative provisions so far as they related to Western Samoa could "not be sensibly

considered without a reference to the general background of the relations between that territory and New Zealand up to the time of the passing of the [1923] Act". The Court began with the German renunciation of right and title to Western Samoa in the Treaty of Versailles and traced the various international, imperial and national measures that were taken to set up the mandate. The Court recorded two propositions that were not disputed by counsel for the person claiming citizenship : the mandate did not cause the inhabitants of the territory to become British subjects and they could not be naturalised under the law in force before 1923. The Court then set out the League resolutions mentioned above, and commented that

In the absence of unequivocal language it is not to be supposed that the New Zealand Parliament would intend to legislate in a manner inconsistent with moral, if not legal, obligations in this sphere ...⁸⁵

The difference between the two courts can be put in terms of the emphasis each placed on particular legislative words and their "unambiguous meaning", on the one side, and, on the other, their context (not just the Mandatory system but also the Imperial one given the exclusive control exercised at that time by the Imperial Parliament over the general grant of British subject status and the still subordinate position of Dominion legislatures) and purpose (relevantly here "to make special provisions for the naturalization of persons resident in Western Samoa" in accordance in fact with agreements reached at the Imperial conferences). While the Privy Council went "straight" to the 1928 Act, the New Zealand Judges looked at it, like its 1923 predecessor, in its broader contexts.⁸⁶ While not denying that they were confined *by* the words of the statute, they did not see themselves as confined *to* them.

At least in part as a result of adopting that different approach, the New Zealand judges were able to give what many - including the two governments - considered was a more accurate account of the relationship between the mandated territory and the mandatory power than that given by the Privy Council, which on the basis of an incomplete reference to one provision of the Mandate (and no other part of the international and imperial background) saw no difficulty in a mandated territory being in essence

⁸⁵ [1979] 2 NZLR 74, 79.

⁸⁶ See the surprising comment by the Privy Council that the 1923 resolution appeared to be inconsistent with the provision in article 2 of the Mandate "that Western Samoa was to be governed as an integral part of the Dominion of New Zealand" ([1982] 1 NZLR 165, 176). I say surprising since the article read as a whole and in context appears to present no inconsistency at all.

under the sovereignty of the Mandatory power.⁸⁷ The more comprehensive contextual approach of the New Zealand judges might be thought more appropriate where constitutional and international elements are central.⁸⁸

5. *International implementation*

The international implementation mechanisms would once have been seen as falling outside my topic, but their rapidly growing significance and the increased public notice of them justifies four brief comments. So too do judicial indications, in respect of the Human Rights Committee and the International Centre for the Settlement of Investment Disputes (ICSID), that in some senses our judicial structure does not end with our national court system.⁸⁹ It is a puzzle that the mechanisms are so often neglected in discussions of our broader legal system.

The first point, by way of repetition, is that New Zealand has been subject to the processes for international implementation and monitoring of its international obligations for all of its independent existence. To the mechanisms already mentioned operating under the International Labour Organisation and the mandate and trusteeship systems, can be added among

⁸⁷ The Governments of New Zealand and Western Samoa found the Privy Council decision unacceptable, and within a month negotiated an agreement which substantially reversed its general effect; see the Protocol of 21 August 1982, AJHR A56, and the Citizenship (Western Samoa) Act 1982. The Privy Council judgment and the governmental and legislative responses were the subject of extensive commentary. For James Crawford "the real difficulty with the decision is that it undermines the assumptions of all parties concerned over a long period of time, assumptions which formed the basis of transactions such as the establishment of the independent State of Western Samoa and the administration (from 1959 onwards) of its separate citizenship legislation" ((1982) 53 BYIL 268).

⁸⁸ Compare for instance Lord Hoffman's discussion of constitutional interpretation for the Privy Council in a recent Mauritius case, *Mutadeen v Pointu* [1998] 3 WLR 18, 25-26, and the structure of another judgment, contemporaneous with the *Lesa* judgment, relating to another important Samoan constitutional issue, *Attorney-General of Western Samoa v Saipa'ia Olomalu* (1982) reported in (1984) 14 VUWLR 275 (Western Samoan Court of Appeal; I was a member of that Court).

⁸⁹ *Tavita v Minister of Immigration* [1994] 2 NZLR 257, 266 and *Attorney-General v Mobil Oil NZ Ltd* [1989] 2 NZLR 649. A Law Commission recommendation to give accurate effect to the ICSID Convention remains unimplemented although the other proposals have been enacted in the Arbitration Act 1996, *Arbitration* (1991 NZLC R20) paras 154-171, 449. The omission of those provisions from the Bill in the course of its passage was not explained by the Select Committee or in the Parliamentary debate.

others the Permanent Court of Arbitration (1900), the League of Nations (1919), the International Court (1931), the United Nations (1945), the International Centre for the Settlement of Investment Disputes (1980), ad hoc arbitrations (as with the *William Webster* case in 1925 and the *Rainbow Warrior* cases in 1986 and 1990), the six human rights treaty committees (from 1972), the International Humanitarian Fact Finding Commission (1991), the Law of the Sea Tribunal and Continental Shelf Commission (1996), and the World Trade Organisation dispute settlement procedures (1995).

That list makes the second point - the wide and increasing range of subject matters in respect of which New Zealand is subject to international monitoring, investigation and judgment.

The third point is about the opportunities that these mechanisms provide for New Zealand, New Zealand individuals and organisations as claimants. That is to be seen in ICJ, ILO, ICSID, WTO and human rights proceedings brought by or against New Zealand, New Zealand organisations and individual New Zealanders. Increasingly, as well, New Zealanders are being elected and appointed to those bodies including at present the WTO dispute settlement body and appellate body, three of the human rights treaty committees, the Commission on the limits of the continental shelf, and the International Humanitarian Fact Finding Commission.

The fourth point is related to the third. Several of the implementation provisions require the State parties, New Zealand included, to report periodically on the action they have taken to give effect to their treaty obligations. That reporting process may provide opportunities to interested bodies to supplement, and help provide a basis for questioning, the official New Zealand position. That opportunity is expressly provided for in the Constitution of the ILO. Practice varies in respect of other reporting processes, but increasingly non-governmental organisations are becoming involved in those reporting processes. This involvement is evidenced in 1998 by the preparation in New Zealand and presentation in New York of the New Zealand government report to the Committee on the Elimination of Discrimination against Women.

V. THE LEGAL PROFESSION AND THE LAW SCHOOLS

My short message for the profession, including faculty and students in the law schools, is that certain old ideas must be slain if we are to do our jobs properly. We have to look more closely at the Westphalian State than many of us have in recent years. We take it too much for granted. We do that

unthinkingly with the comfort of the clearly stated thoughts of Dicey and of Hall and others like them. We should realise that their ideas are relatively new - as indeed is the Westphalian State which is, for instance, only half the age of the University.⁹⁰ Those ideas are not immutable.

I wonder whether some of those in the very place about which Dicey made his famous statement about the power of Parliament have yet to see the real significance of what the members of the judicial committee of one chamber of that institution said in 1990 when Lord Bridge, in an understated way, recorded a constitutional revolution:

Some public comments on the decision of the European Court of Justice, affirming the jurisdiction of the courts of member states to override national legislation if necessary to enable interim relief to be granted in protection of rights under Community law, have suggested that this was a novel and dangerous invasion by a Community institution of the sovereignty of the United Kingdom Parliament. But such comments are based on a misconception. If the supremacy within the European Community of Community law over the national law of member states was not always inherent in the E.E.C. Treaty (Cmnd. 5179-II) it was certainly well established in the jurisprudence of the European Court of Justice long before the United Kingdom joined the Community. Thus, whatever limitation of its sovereignty Parliament accepted when it enacted the European Communities Act 1972 was entirely voluntary. Under the terms of the Act of 1972 it has always been clear that it was the duty of a United Kingdom court, when delivering final judgment, to override any rule of national law found to be in conflict with any directly enforceable rule of Community law. Similarly, when decisions of the European Court of Justice have exposed areas of United Kingdom statute law which failed to implement Council directives, Parliament has always loyally accepted the obligation to make appropriate and prompt amendments. Thus there is nothing in any way novel in according supremacy to rules of Community law in those areas to which they apply and to insist that, in protection of rights under Community law, national courts must not be inhibited by rules of national law from granting interim relief in appropriate cases is no more than a logical recognition of that supremacy.⁹¹

⁹⁰ Many of course date the modern State and interstate system from the signing of the Treaties of Westphalia of exactly 350 years ago (n 12 above). See eg the choice by Clive Parry of those treaties as the foundation and starting point of his *Consolidated Treaty Series* (1648-1919) which, with the *League of Nations* and *United Nations Treaty Series* in well over 2000 volumes, provide us with much of the formal interstate law of the world. See also Leo Gross "The Peace of Westphalia" (1948) 42 AJIL 20.

⁹¹ *R v Secretary of State for Transport, Ex parte Factortame Ltd* (no 2) [1991] 1 AC 603, 658-659; see also *R v Secretary of State for Employment, Ex parte Equal Opportunities Commission* [1995] 1 AC 1, 26-27, both discussed in "Sovereignty: a legal perspective"

Thinking about the position of practitioners, academics and students, consider the legal systems in which clients, especially those involved in trade or business or communications or intellectual property or finance, or the movement of families and individuals, really operate. Where are the relevant powers? Where is the law made? Where are powers of decision and enforcement exercised? If we think that our law is an island entire unto itself, can we really understand the ways in which law operates today, or serve those clients, or teach those who will serve those clients? I trust that by now my answers to those questions are clear.

Consistent with those answers is the resolution adopted last year by the Institut de Droit International, about the teaching of international law. The Institut:

Emphasising that international law increasingly affects the content of municipal law and that a knowledge of international law is necessary to discharge a wide range of professional responsibilities at the national level and the responsibilities of individuals in an increasingly cohesive international society;

Reaffirming that, in the conditions prevailing in the present world, legal education is incomplete if it does not cover the basic elements of public and private international law;

Noting that the international community is moving to a more complex system in which non-State actors are increasing in importance and that international and national laws are becoming more closely interrelated;

Anxious to ensure that the teaching of international law is sufficiently adapted to changes in the international system and to the role and interests of various non-State actors, including individuals.

Recommends that:

1. Every school and faculty of law offer a foundation course or courses on public and private international law. The purpose of such courses is to familiarise students with the basic elements of public and private international law and to provide a foundation on which more specialized knowledge can be acquired at later stages of the educational process.

2. No law student graduate from schools or faculties of law or enter the practice of law and the judicial or diplomatic service without having had a foundation course or courses on public and private international law.⁹²

in G A Wood and L S Leland Jr (eds) *State and Sovereignty. Is the State in Retreat?* (1997) 83-88.

⁹² See also the remainder of the resolution, including its appendices and the background material, in 67(1) *Annuaire* 121-217; and the debate on the proposed resolution in 67(2) *Annuaire* 83-193.

I would go further and emphasise the importance of international legal materials being integrated into the regular subjects of the curriculum. National legal systems cannot be adequately understood unless they are firmly seen in their international context. Again I return to the last century to help make my point. Towards the end of a life time in the law, including being the leading judge in New York, Chancellor James Kent returned to the University to teach budding lawyers at Columbia College. His lectures were published in the enormously influential *Commentaries on American Law*, the first edition in 1826. He began not with the law of New York (city or state) nor with the law of the United States, but with “the law of nations”. The faithful observance of that law, he said, is essential to the national character and the happiness of humanity. Even his contrasting references to nation and to humanity help make my point.

To be concrete about the New Zealand situation, I refer to five standard subjects of the law curriculum:⁹³

- do legal system courses follow Kent’s advice, generally or in concrete contexts (for instance in respect of international and colonial practice relating to indigenous rights and the extension of empire, around the time he was writing, if the Treaty of Waitangi is to be understood as a product of its time)?
- do contract courses discuss the United Nations Sales Convention, the Conventions on the Carriage of Persons and Goods and standard terms prepared by the International Chamber of Commerce and others which between them cover much of the contractual activity reflected in New Zealand’s GDP?
- do family law courses consider intercountry adoption, international abduction of children, international enforcement of maintenance orders, relevant general treaties (on children, discrimination against women and human rights) as well as the issues relating to the recognition of foreign status?
- do equity courses consider the conventions on the formal validity of wills and the administration of deceased estates?
- do commercial law courses consider transnational investment protection, transnational insolvencies and international commercial arbitration - as well as the relevant parts of the public law of international trade which bear directly on private traders?⁹⁴

⁹³ I have not chosen those such as labour law, taxation and environmental law in which the international element is obvious.

⁹⁴ I should make it clear that I am not contending that every skerrick of relevant international law should be included in every course. No law programme can be

I conclude with another great nineteenth century thinker - this time a novelist - who developed or rather anticipated Oliver Wendell Holmes' metaphor about movement, felt and unfelt, by reference to astronomy and history. In his last chapter of *War and Peace*, Leo Tolstoy mentioned the long and stubborn struggle between the old Ptolemaic views of the universe and the new Copernican one.

Theology stood on guard for the old views and accused the new of violating revelation. But when truth conquered, theology established itself just as firmly on the new foundation.

Just as prolonged and stubborn is the struggle now proceeding between the old and new conception of history, and theology in the same way stands on guard for the old view and accuses the new view of subverting revelations.

Just as in astronomy it was necessary to renounce the consciousness of an unreal immobility and to recognise an unfelt motion it is similarly necessary to renounce a freedom that does not exist, and to recognise a dependence of which we are not conscious.

completely comprehensive nor should it try to be. What is required is a sense, arising from some examples, of the integral character of international law in our national law.

FUNDING THE REMEDIATION OF CONTAMINATED LAND IN AUSTRALIA AND NEW ZEALAND: THE PROBLEM OF ORPHAN SITES

BY ANNA KINGSBURY*

I. INTRODUCTION

Land contamination from the use of hazardous chemicals is a matter of public concern in both Australia and New Zealand. If not cleaned up, contaminated sites can pose serious long-term risks to health and to the environment.¹ There are now significant numbers of “orphan” contaminated sites, for which no party is clearly responsible. The arguments for clean up of such sites are compelling, but the legal and economic issues surrounding financial liability are commonly perceived as complex and uncertain, and neither the public nor the private sector exhibits much readiness to pay the costs. As a consequence, governments have been reluctant to take the difficult political decisions required, and the problems remain unresolved. Neither Australia nor New Zealand has a comprehensive approach to liability or to site remediation, either at national or at state level.

This article reviews and clarifies the issues surrounding financial liability for clean up of contaminated land in Australia and New Zealand, focusing particularly on orphan sites. It examines the existing legal regimes for apportioning liability, and argues that there is now an urgent need for a comprehensive national strategy for dealing with orphan site remediation in both countries.

II. CONTEXT: THE PROBLEM OF LAND CONTAMINATION

Land contamination typically derives from the use of hazardous chemicals and compounds in industrial and agricultural processes. Cleaning up contaminated land is an increasingly urgent and expensive problem, one

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¹ The Australian and New Zealand Environment and Conservation Council (ANZECC) defined a contaminated site as “a site at which hazardous substances occur at concentrations above background levels and where assessment indicates it poses, or is likely to pose, an immediate or long-term hazard to human health or the environment”. Background levels refer to ambient levels of a contaminant in the local area of the site under consideration (ANZECC and the National Health and Medical Research Council (NHMRC), *Australian and New Zealand Guidelines for the Assessment and Management of Contaminated Sites* (1992) 2).

which has received growing public attention internationally in the last three decades, as the extent of contamination has become known. In the United States, over 35,000 contaminated sites have been reported to the Environmental Protection Agency, and many more have been nominated as potentially contaminated. The average cost of a site clean up is estimated at between US\$29 million and US\$35 million.² In the United Kingdom, it is estimated that dealing with contaminated derelict land alone will cost at least GBP20 billion.³ Similar situations exist in Europe.⁴

The problem in Australia and New Zealand is fortunately on a much smaller scale, although the precise number of sites is unknown.⁵ The Australian and New Zealand Environment and Conservation Council (ANZECC) estimates that there are up to 10,000 such sites across Australia.⁶ Other estimates suggest that there are 20,000 potentially contaminated sites in Victoria alone,⁷ and it is estimated that in New South Wales there are 7,000 sites requiring clean up.⁸ In New Zealand, 8,000 sites have been identified as potentially contaminated, of which 1,500 are thought to be high risk sites.⁹ The cost of clean up of the high risk sites alone is estimated at NZ\$600 million.¹⁰

² Greenwood, "Looking Ahead: Environmental Regulation - A Future?" in Boyle, A (ed) *Environmental Regulation and Economic Growth* (1994) 99, 125.

³ Cridland, "Meeting the Cost of Environmental Regulation" in Boyle, supra note 2, at 233, 238.

⁴ There are over 50,000 potentially contaminated sites in West Germany and over 100,000 in the Netherlands (ANZECC and NHMRC, supra note 1, 1).

⁵ Rowe and Seidler "Introduction" in Rowe, G and Seidler, S (eds) *Contaminated Sites in Australia: Challenges for Law and Public Policy* (1993) xvii, xvii-xviii.

⁶ ANZECC and NHMRC, supra note 1, 1.

⁷ Taylor, "Contaminated Sites in Tasmania" in Department of Environment and Planning and Stephenson EMF Consultants (eds), *Contaminated Sites Conference Proceedings* (1992) 3.

⁸ Carter, "Hazardous Waste And Contaminated Sites: The North American Experience" in Department of Environment et al, supra note 7, 20-21.

⁹ High risk sites are those which pose an actual or imminent significant adverse effect to human health and the environment (New Zealand Ministry for the Environment, *Discussion Document on Contaminated Sites Management: Liability Issues, Management of Orphan Sites, Role of Local Government* (1995) 2, 31). See also New Zealand Ministry for the Environment, *Potentially Contaminated Sites in New Zealand: A Broad Scale Assessment* (1992) 6.7.

¹⁰ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, 31. See also New Zealand Ministry for the Environment, *Potentially Contaminated Sites*, supra note 9, 6.3.

Orphan sites are sites where contamination has occurred, and clean up is required, but where there is no solvent party liable to pay for remediation work. This may be because all potentially responsible parties are exempt from liability, because they cannot be located, or because they are insolvent or otherwise unable to pay.¹¹ While some orphan sites in Australia and New Zealand have been cleaned up, this has been on an ad hoc basis.¹² And there has until recently been very little detailed research work done on either methods of remediation or legal and policy frameworks for arranging and funding remediation.

III. POLICY ISSUES IN THE REMEDIATION OF ORPHAN SITES

In Australia, any approach to funding orphan site remediation should comply with the principles agreed in the May 1992 Inter-Governmental Agreement on the Environment (IGAE) and the December 1992 National Strategy for Ecologically Sustainable Development. Relevant agreed principles include:

- (i) ecologically sustainable development;
- (ii) precautionary principle;
- (iii) intergenerational equity;
- (iv) conservation of biological diversity and ecological integrity;

¹¹ The ANZECC has considered issues of financial liability for clean up, including clean up of orphan sites. The ANZECC defines orphan sites as: "existing and future sites for which either: (i) those who might be liable for the contamination cannot be found, cannot pay clean up costs or no longer exist, or (ii) it has been decided by the government that the person(s) responsible or who otherwise might be liable for the contamination should not bear any of the costs of remediation; and in either case, the costs of remediation must be met in some other way determined by government" (ANZECC, *Financial Liability for Contaminated Site Remediation: A Discussion Paper Prepared by the Australian and New Zealand Environment and Conservation Council* (1993) 37).

¹² Osmer, "Cleaning Up Contaminated Land: Who Pays?" in Rowe and Seidler, *supra* note 5, at 181, 182. See also New Zealand Ministry for the Environment, *Discussion Document*, *supra* note 9, 31. Such ad hoc clean ups have mainly been undertaken where contamination poses a serious risk to public health. For example, the New Zealand Government has funded some clean up work at a Hanmer Springs children's camp site which was found to be contaminated with timber treatment chemicals. In other cases, for example a former chemical factory site at Mapua, local authorities have agreed to share the costs of the clean up with the government. See Alice Taylor, "Government to Pay for Pollution Cleanup" *Evening Post* 8 July 1995, 8.

(v) improved valuation pricing and incentive mechanisms, incorporating the polluter pays principle.¹³

The ANZECC considered the application of these principles to contaminated site remediation in its Position Paper of April 1994.¹⁴ It set out the following principles as meeting these criteria:

- (i) equity: the liability regime should seek to treat parties fairly and justly, with evenhandedness and impartiality;
- (ii) effectiveness: the regime should minimise risks to human health and the environment and achieve the desired outcome of timely clean up to appropriate levels;
- (iii) efficiency: the regime should ensure that the funds are directed to the maximum extent possible towards achieving the above outcome at the lowest possible cost to society. This will be reflected by a liability regime which reduces uncertainty to the maximum extent practicable, is administratively simple and consistent across jurisdictions. The regime should aim to discourage the need for litigation and other dispute resolution mechanisms, especially before remediation occurs, and minimise the need for commitment of public funds for this;
- (iv) prevention of future pollution: the regime should ensure that polluters bear primary liability for remediation of sites they have contaminated, thereby discouraging future contamination.¹⁵

The New Zealand Ministry for the Environment issued a Discussion Document on contaminated sites management in November 1995, in which it also considered the policy objectives or principles which should underlie any liability regime for contaminated site remediation.¹⁶ In the paper, the Ministry considered particularly the policy objectives to be achieved through any regime for funding of orphan site clean up.

The New Zealand Government agreed that funding options for clean up of orphan sites should be assessed principally on the basis of the following criteria:

- (i) minimising the incentive to create new orphan sites;
- (ii) implementation of the polluter pays principle;

¹³ *Inter-Governmental Agreement on the Environment* (1992) Schedule section 3.

¹⁴ ANZECC, *Financial Liability for Contaminated Site Remediation: A Position Paper* (1994) 5.

¹⁵ ANZECC, *supra* note 14, at 5-6.

¹⁶ New Zealand Ministry for the Environment, *Discussion Document*, *supra* note 9.

- (iii) efficiency of revenue collection;
- (iv) distribution of benefits;
- (v) equity aspects;
- (vi) practicality.

These criteria broadly echo those in the ANZECC Position Paper, suggesting that there is agreement on policy objectives to be achieved. Implementation of these objectives is more contentious, as the principles are open to interpretation, and various stakeholders support alternative interpretations.

One difficulty acknowledged by the ANZECC is that there is potential for conflict between the goals of equity and efficiency. This conflict raises particular difficulties in the case of orphan sites, where the concern is the financial consequences of a past event.¹⁷

The goal of economic efficiency is forward-looking, in the sense that efficient allocation of resources is achieved where the costs of pollution are fully internalised, rational decisions can be made, and costs can be passed on to consumers. The success of this approach depends upon internalising externalities, such as free access to water and air, and minimising transaction costs, as might be associated with industry levies, for example.¹⁸

Thus, in the case of contamination, the goal of economic efficiency is in general harmony with the polluter pays principle. Where the polluter is liable for the costs of pollution, the polluter has an incentive to prevent pollution, and pollution costs can be internalised.

Retrospective polluter liability for contaminated sites arguably does not achieve this goal of economic efficiency, as the decision leading to the pollution has already been made. Costs cannot be internalised and passed on, except retrospectively.

But it is also arguable that making the polluter retrospectively liable for contamination does serve the goals of equity and distributive justice. The polluter caused the pollution, and it is just that the polluter should be at least partially liable for remediation, although liability may be shared with other beneficiaries.

¹⁷ Callaghan, Catherine *The Liability of Lenders for Remediation of Contaminated Sites Under the Resource Management Act 1991* (1995) 43.

¹⁸ *Ibid.*, at 38-40.

In designing regimes for assigning liability and funding clean up, a balance should be struck between the competing goals of equity and efficiency. In so doing, sufficient flexibility should also be retained to avoid inequities for individuals.¹⁹

IV. IDENTIFICATION OF ORPHAN SITES: LIABILITY ISSUES

The number of sites classified as orphan will be determined by the regime for determining liability for clean up. And the cost of clean up will likewise vary, depending on the number of sites so classified. In both Australia and New Zealand liability for clean up can arise under common law, or by statute.

A. Common Law Liability

At common law, liability may arise under an action in negligence, in public or private nuisance, or under the *Rylands v Fletcher*²⁰ principle.

These remedies are limited in practice by the problems associated with all such actions, where plaintiffs require resources in order to get access to justice.²¹ The remedies have other limitations in contaminated land cases.²² They are open only to persons or land owners who suffer harm to property, and are not generally available to members of the public at large.

Negligence requires the plaintiff to establish that a duty of care is owed to the plaintiff by the owner or occupier, that that duty has been breached, and that there has been damage that is not too remote. A defence of reasonable care is available. Further, in land purchases, the seller owes no general duty to the buyer and is not generally liable to the buyer for contamination at the time of transfer.

In nuisance and *Rylands v Fletcher* actions, liability arises only for damage which is reasonably foreseeable.²³ *Rylands* applies only where there is a

¹⁹ ANZECC, *supra* note 14, at 6.

²⁰ *Rylands v Fletcher* (1868) LR 3 HL 330.

²¹ Shanahan, 'The Scales of Justice are Twisted and Crooked: A Public Interest Law Perspective on Tort' in Rowe and Seidler, *supra* note 5, at 149, 150.

²² Palmer, "Contaminated Land Liability: UK and New Zealand Comparisons" (1996) 1(16) *Resource Management Bulletin* 201, 202; and Taberner "Civil Liability: Recent Statutory Measures" in Rowe and Seidler, *supra* note 5, at 145-152.

²³ *Cambridge Water Co v Eastern Counties Leather plc* [1994] 2 AC 264.

non-natural use of land.²⁴ In nuisance, successors in title are not responsible unless they are found to have adopted the nuisance, in which case there is a duty to mitigate.²⁵

Rylands v Fletcher originally imposed strict liability. But the courts have demonstrated an increasing reluctance to impose strict liability for contamination at common law. As environmental law is perceived as being of growing public interest and importance, courts are preferring to leave it to parliaments to impose liability by legislation.²⁶ For these reasons, statutory frameworks for liability are generally more significant than common law liability.

B. Statutory Liability

1. Existing legislative schemes

A variety of legislative schemes for determining clean up liability currently exist in Australia and New Zealand. These schemes generally adopt the “command and control” approach to environmental regulation, prescribing behaviour rather than using market-based incentives and flexible contract-based mechanisms.²⁷

The following table represents the existing liability for clean up of contaminated land in Australia and New Zealand.²⁸

²⁴ Non-natural use is open to various interpretative approaches. See *Cambridge Water Co v Eastern Counties Leather plc* [1994] 2 AC 264, and Burnett-Hall, “Emerging Trends in Environmental Law” in Thomas, P (ed) *Environmental Liability* (1990)149, 153.

²⁵ Palmer, supra note 22, at 202.

²⁶ *Cambridge Water Co v Eastern Counties Leather plc* [1994] 2 AC 264, 305; *Burnie Port Authority v General-Jones Pty Ltd* (1994) 68 ALJR 331; and McDonald “Financial Liability for Contaminated Site Clean ups - The Increasingly Strict Standard of Fault-Based Liability” (1994) 11(6) *Environmental and Planning Law Journal* 516.

²⁷ Stewart, “The Future of Environmental Regulation” (1996) 15 *Journal of Law and Commerce* 585-595, and Bruce Parry, *Environmental Law: A Guide to Concepts* (1996) 32-33. Note that there are some initiatives toward more flexible approaches, for example the Victorian Environment Protection Act provides for Accredited Licensees.

²⁸ ANZECC, supra note 14, 29-30.

	QLD	SA	VIC	NSW	WA	TAS	NT	ACT	NZ
Polluter	Yes	Yes	Yes	Yes	Yes	N/A	N/A	N/A	Yes
Occupier	No	Yes	Yes	Yes	Yes				Yes
Owner	Yes	Yes	If occupier	No	Yes				Yes
Remediation Liability	Strict	Fault based	Absolute	Strict	Strict				?

Notes:

(i) In New Zealand, there are differing views on whether liability under the Resource Management Act 1991 is retrospective, and whether liability is strict. The government has announced an intention to introduce legislation to establish a liability framework.²⁹

(ii) New South Wales has proposed an amendment extending liability to controllers, including owners and mortgagees in possession.³⁰

(iii) Tasmania has announced plans to legislate in line with the ANZECC recommendations.³¹

The variety of legislative schemes currently produce different outcomes, because of differences in the wording of the statutory provisions, and because of differing judicial interpretations. As a result, a site that would be classified as orphan in one jurisdiction would not be orphan in another. There is therefore an urgent need for a consistent approach in order to advance the prospects of remediation, and to provide certainty for industry and investors.

2. Issues in law reform

There is no national consistency in legislation in ANZECC jurisdictions, and a number of issues arise in developing a consistent regime.

(a) Retrospective application

Environmental statutes in Australia and New Zealand generally contain provisions assigning liability for future contamination of land,³² which

²⁹ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, 8-9; and Palmer, supra note 22, 203.

³⁰ Glindemann, "Proposed Changes to New South Wales and Tasmanian Contaminated Site Regimes" (1997) 25(1) *Australian Business Law Review* 69, 70.

³¹ *Ibid*, at 71.

³² Examples include Resource Management Act 1991 (NZ) and Environmental Protection Act 1970 (Vic).

reduces the likelihood of future orphan sites (except arguably in the case of company asset stripping and insolvency).

Liability regimes for past contamination are more complex, and raise questions of retrospective operation of legislation. It is arguable that it is unjust to impose liability for activities which caused pollution where these activities were lawful at the time but do not meet today's standards. This "lawful polluter" argument can be extended to suggest that, since governments and taxpayers allowed or in some cases promoted the polluting activities, they should therefore be liable for part or all of the cost of remediation.³³

There is an obvious conflict between the lawful polluter argument and the polluter pays principle. As discussed, the polluter pays principle is most appropriate for the prevention of future pollution, rather than as a basis for holding polluters liable for remediating sites contaminated in the past. The ANZECC acknowledges that the polluter pays principle operates most effectively where environmental costs can be internalised by industry so that costs are reflected in the price of goods or services produced.

However, the ANZECC recommended polluter liability as "a clear message that social costs generated by polluters will be borne by polluters".³⁴ The polluter, rather than the owner or occupier, should therefore be liable, even where some element of retrospectivity is involved. This does not mean that criminal liability will be imposed for previously lawful activity.³⁵

(b) Liable parties

The polluter pays principle means that, wherever possible, the actual polluter should "be the party held liable for remediation of contaminated sites, and associated costs, such as assessment and auditing".³⁶ The principle is accepted by the ANZECC,³⁷ and statutory regimes generally assign liability to polluters in some form, although the precise interpretation of the principle varies across jurisdictions.³⁸

³³ ANZECC, *supra* note 14, at 23.

³⁴ *Ibid*, at 6.

³⁵ *Ibid*, at 8. In New Zealand, criminal liability would be contrary to the New Zealand Bill of Rights 1990 (New Zealand Ministry for the Environment, *Discussion Document*, *supra* note 9, at 9).

³⁶ ANZECC, *supra* note 14, at 14.

³⁷ *Ibid*, at 8.

³⁸ The polluter pays principle is accepted by OECD nations (ANZECC, *supra* note 11, at 14).

Where the polluter cannot pay, other parties may be assigned liability for clean up. The current owner or occupier of the site can be liable for clean up. The ANZECC recommends that, “where the polluter is insolvent or unidentifiable, the person in control of the site, irrespective of whether that person is the owner or the current occupier, should be liable, as a general rule, for the costs of any necessary remediation”.³⁹ The rationale is that the owner or occupier has the legal power to arrange remediation, and would receive the most benefit from such remediation.

It has been argued that lenders should be liable for remediation, as financiers of the polluting activity, and as the party most likely to be in a position to pay for clean up. Lender liability was imposed in the United States under the Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA),⁴⁰ based on the argument that those with the “deepest pockets” should fund clean up. Lenders are liable where they participate in the management of the debtor’s activities.⁴¹ Canadian and United Kingdom legislatures have also made provision for lender liability.⁴² In Australia and New Zealand, lender liability may arise under various legislative provisions.⁴³

The banking and financial sectors oppose lender liability, arguing, *inter alia*, that:

- (i) it will severely restrict available finance as lenders adopt a conservative approach, and the cost of finance will rise.
- (ii) lenders are not regulators. Regulation is a government function. Lenders rely on government environmental approvals.
- (iii) lenders are not insurers, and are not in a position to assess environmental risks.

³⁹ ANZECC, *supra* note 14, at 9.

⁴⁰ Pub L 96-510 (1980), 42 USC 9601 (USA). CERCLA is also commonly known as “Superfund”.

⁴¹ Mfodwo, “Current Developments in Lender Liability” in Rowe and Seidler, *supra* note 5, at 163, 164; Smith and Monaghan, “The Impact of Environmental laws on Transactions” in Thomas, *supra* note 24, 286-7; and Clark, *S Lender Liability for Contaminated Sites Remediation: Some Recent Trends* (1991).

⁴² Ontario’s Environmental Protection Act RSO 1980 c.141 is an example. See Callaghan, *supra* note 17, 25-6, and Mfodwo, *supra* note 41, at 164.

⁴³ NSW, Victoria, Queensland and New Zealand legislation all have potential avenues for lender liability (Mfodwo, *supra* note 41, at 164). For example, in Victoria a mortgagee in possession who is, or appoints, a controller of the premises, may be liable as an “occupier” (Environment Protection Act 1970 (Vic) s4(3)).

(iv) lenders are not responsible for the contamination, and are generally not in a position to control environmental effects.⁴⁴

The ANZECC recommends that lenders should not be liable where they act solely as the holder of a security interest in the site and have taken no steps to enforce that security. However, where they have either caused the contamination, or have assumed control of the site, they should be liable.⁴⁵

It has been suggested that other third parties should be liable where they are involved in the management of the site, for example, lawyers, accountants, engineers and other professionals.⁴⁶ Such liability would depend on the level of involvement in the contaminating activities, and can be incurred under principles of professional negligence.⁴⁷

(c) Apportionment of liability

In many cases, liability can attach to more than one party, raising the question of how such liability should be apportioned. In the United States under CERCLA, liability is joint and several, leading to widespread litigation between potentially responsible parties, and between parties and insurers, and parties and government.⁴⁸ As a result, remediation is delayed, and funds for remediation are diverted into litigation.⁴⁹ Typically, clean up of a site in the US takes 7-9 years.⁵⁰ A 1993 RAND Corporation study estimated that transaction costs account for 27% of total costs of clean up.⁵¹ The United States model is therefore not seen as a desirable one to be followed in Australia and New Zealand.

The ANZECC recommends that liability between parties should be apportioned according to their contribution to contamination, and that this should be determined by the tribunal of fact. However, joining of other parties should not delay clean up, and must be subject to such action being

⁴⁴ Australian Bankers' Association, *Position Paper: Banks and the Environment* (1992).

⁴⁵ ANZECC, *supra* note 14, at 15. Victoria's Environment Protection Act takes this approach.

⁴⁶ ANZECC, *supra* note 11, at 30.

⁴⁷ ANZECC, *supra* note 14, at 21. ANZECC, *supra* note 11, at 30.

⁴⁸ Saul and Janisson, "Contaminated Site Clean Up: Is Superfund the Answer?" (1994) 1(2) *Butterworths Resource Management Bulletin* 18, 19; Smith and Monaghan, *supra* note 41, at 284; Ludwizewski, "Superfund: The United States Response to Hazardous Waste Sins of the Past" in Rowe and Seidler, *supra* note 5, at 62-63.

⁴⁹ Saul and Janisson, *supra* note 48, at 20.

⁵⁰ Ludwizewski, *supra* note 48, at 60.

⁵¹ Saul and Janisson, *supra* note 48, at 20; and Ludwizewski, *supra* note 48, at 62-63.

taken first.⁵² The ANZECC also recommends that there be a statutory right to recover clean up costs from other potentially liable parties.⁵³ It remains to be seen whether this approach might not also lead to extensive litigation, but, if it does, it will be after the clean up, so that the parties will not be motivated by a desire to delay.

(d) Basis of liability

There are different approaches which might be taken to determining liability by statute.

Under a fault-based approach, liability attaches where there is a duty of care, a particular standard of care is expected, and damage or harm is caused by intentional, reckless or negligent action. This is similar to common law negligence. Under this approach potentially responsible parties could escape liability if:

- (i) there was no duty of care; or
- (ii) there was no breach of the duty of care; or
- (iii) the breach did not cause the damage; or
- (iv) the damage was not reasonably foreseeable.

Thus, liability would be difficult to establish, as it is under common law, and there would consequently be more orphan sites. This approach would reduce the range of situations in which liability would arise. It consequently has support from industry groups,⁵⁴ but is not favoured by the ANZECC.⁵⁵

An alternative is the risk-based approach to liability, whereby anyone receiving a benefit from contaminating activities would be potentially liable for remediation. Liable parties could therefore include lenders, and arguably the community as a whole. Risk-based liability is also referred to as the “beneficiary pays” approach.⁵⁶

Combinations of risk and fault-based liability are also possible, so that, for example, liability is greater where there is an element of fault.

Strict liability is the approach favoured by the ANZECC for polluters, owners and occupiers.⁵⁷ Strict liability allows for quick determination of liability with reduced likelihood of litigation, and it applies the polluter pays

⁵² ANZECC, *supra* note 14, at 11.

⁵³ *Ibid.*, at 10.

⁵⁴ *Ibid.*, at 18.

⁵⁵ *Ibid.*, at 9.

⁵⁶ Parfy, *supra* note 27, at 35-37.

⁵⁷ ANZECC, *supra* note 14, at 9.

principle. Strict liability also reduces the likelihood that sites will be orphaned. Appeal rights should exist for situations where strict liability is inequitable, for example, where a householder with limited resources has unknowingly bought contaminated land.

(e) Summary

The ANZECC recommends:

- (i) governments should ensure that the polluter, where solvent and identifiable, is liable for remediation.
- (ii) where the polluter is insolvent or unidentifiable, the person(s) in control of the site, irrespective of whether that person is the owner or the current occupier, should be liable. Parties should be liable according to the level of their contribution to the contamination.
- (iii) liability should be strict.
- (iv) owners, occupiers, polluters, or public authorities who undertake clean up have a statutory right of recovery of costs of clean up, from the polluter or others who exacerbated the situation.
- (v) lenders holding security over a risk site should have a clear choice of courses of action, and liability will only attach if the lender assumes control of the site.⁵⁸

The ANZECC recommendations are moderate, and strike a balance between equity and efficiency in allocating liability and identifying those sites which are orphan. The recommendations avoid the “deep pockets” approach adopted in the United States, and the likelihood of litigation inherent in joint and several liability. The recommendations should be implemented by legislation in the various jurisdictions, as a prerequisite to a national approach to remediation of contaminated lands and identification and remediation of orphan sites.

V. RESPONSIBILITY FOR FUNDING REMEDIATION OF ORPHAN SITES

There is continuing debate about who should fund remediation of orphan sites. In Australia, the issue is whether remediation is more appropriately a responsibility of Commonwealth, State or local governments. In New Zealand, a more limited debate centres around whether clean up is a central or local government responsibility.⁵⁹

⁵⁸ Ibid, at 2-3, 4-16.

⁵⁹ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, at 33-34.

In Australia, environmental and land use issues are traditionally regarded as a responsibility of State government.⁶⁰ State governments are in the best position to assess the need for clean up, and the direct benefits of a clean up are principally experienced by the States.⁶¹ Clean up would therefore appear to be a State responsibility.

However, the Commonwealth has increasingly assumed responsibility for environmental matters, relying, *inter alia*, on the external affairs, corporations, and overseas trade and commerce powers of the constitution.⁶² More recent developments, such as the Inter-Governmental Agreement on the Environment 1992 and the establishment of the Commonwealth Environment Protection Agency and the National Environment Protection Authority, suggest an expanded Commonwealth role as States take a co-operative approach to environmental matters.⁶³

The Commonwealth has not taken a national approach to clean up of orphan sites. But there are strong arguments that funding orphan site clean up is a national responsibility, based on principles of equity, uniformity, effectiveness and efficiency.

First, the cost of remediation is likely to be considerable.⁶⁴ It has been suggested that the revenue base of at least one State (South Australia) will be insufficient to raise the revenue required.⁶⁵

Secondly, the Commonwealth government has constitutional powers to raise funds via taxation that are not available to State governments, and has administrative functions with the potential to influence polluter behaviour and provide incentives for remediation.⁶⁶

Thirdly, contaminated sites are not distributed equitably across all jurisdictions. If States are to be responsible for revenue raising, the costs of

⁶⁰ Fisher, D *Environmental law: Text and Materials* (1993) 45-47; and Osmer, *supra* note 12, 182.

⁶¹ New Zealand Ministry for the Environment, *supra* note 9, at 33.

⁶² Fisher, *supra* note 60, at 46-47.

⁶³ *Ibid*, at 50-51, and *Inter-Governmental Agreement on the Environment* (1992).

⁶⁴ In New Zealand it has been estimated that clean up of all high-risk sites will cost NZ\$600 million, of which some NZ\$200 million could conceivably be required for orphan sites (New Zealand Ministry for the Environment, *Discussion Document*, *supra* note 9, at 32).

⁶⁵ ANZECC, *supra* note 11, at 38.

⁶⁶ ANZECC, *supra* note 14, at 14.

clean up will not fall equitably across the country. However, this uneven distribution of sites is partly the result of historical factors, and partly the result of different legislative regimes establishing liability, so that a site that would be classified as orphan in one jurisdiction would not be orphan in another. This raises a difficulty if the Commonwealth is to fund clean up, as it could lead to inequities in the distribution of funds across States.⁶⁷ Because of this variation in liability regimes across ANZECC jurisdictions, the ANZECC recommended in 1994 that the means of providing funding for the remediation of orphan sites should be determined by each of the governments concerned.⁶⁸ A uniform approach to liability would therefore be a prerequisite for Commonwealth funding.

Fourthly, it is in the national interest that sites be cleaned up. All states and territories possess contaminated sites, and the effects of these sites are not necessarily contained within state boundaries. It is a national problem, and it is most effectively addressed consistently at a national level.⁶⁹

Fifthly, assessment and guidelines for remediation are already being addressed on a national basis. Logically, funding could also be so addressed.⁷⁰

Sixthly, consistent nationwide approach to liability for clean up would provide certainty for industry and business, especially for businesses which operate across jurisdictions.⁷¹

For the above reasons, it is argued that the Commonwealth government in Australia and the central government in New Zealand should be responsible for developing a consistent, equitable and efficient regime to be applied to the funding of remediation of orphan sites nationwide.

The ANZECC has made two recommendations relevant to orphan site remediation:

⁶⁷ It is for this reason that the ANZECC recommends that funding should be determined by the governments concerned (ibid, at 14).

⁶⁸ Ibid (Recommendation 12).

⁶⁹ In New Zealand, there is also concern that New Zealand's "clean green" environmental image might be tarnished internationally by the existence of unremediated sites, with consequences for export and tourist industries (New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, at 33.

⁷⁰ Osmers, supra note 12, at 183.

⁷¹ ANZECC, supra note 11, at 5.

- (i) governments should be responsible for ensuring that the necessary remedial action to minimise risks is taken in the case of orphan sites posing risks; and
- (ii) means of providing funding for the remediation of orphan sites need to be determined by the governments concerned.⁷²

The ANZECC stopped short of recommending a national scheme for funding clean up of orphan sites. This was not because a national scheme was seen as undesirable, but because of the expressed concern that, because jurisdictions differed in their liability regimes, any national scheme for funding clean up would be inequitable.⁷³ It is therefore arguable that a preferable solution would be a national scheme for both liability and clean up. Indeed, this was the professed aim of the ANZECC strategy for contaminated sites.⁷⁴

VI. FUNDING REMEDIATION OF ORPHAN SITES

There are various options for funding clean up of orphan sites. All involve the establishment of a fund from which monies can be disbursed to pay for remediation as required. There is continuing debate about how such a fund should be constituted and administered.

A. Sources of Funds

1. Funding from consolidated revenue

Government could establish a fund using monies from consolidated revenue. These funds are raised by governments through a variety of mechanisms, the most significant of which are income and company taxes (and in New Zealand through goods and services tax).

Administrative and compliance costs of raising revenue in this way are very low. No new tax instrument is required, and the establishment of a new, separately administered fund may be unnecessary.

The use of consolidated funds for remediation would represent an acknowledgment that remediation is a community responsibility where the polluter cannot pay, and that the cost should be spread across the community as a whole. Spreading the tax burden in this way would minimise the impact

⁷² ANZECC, *supra* note 14, at 3.

⁷³ *Ibid*, at 14.

⁷⁴ *Ibid*, at 2.

on industry, and there would be little likelihood of individual or company behaviour being modified in a distortionary way.⁷⁵ This is the source of funds generally favoured by industry groups.⁷⁶

However, the use of consolidated revenue is contrary to the polluter pays principle. It spreads the costs across the community rather than targeting polluters. It thereby provides no incentive for polluters to avoid future pollution, but rather subsidises inefficient industry practice, and does not encourage internalisation of costs.⁷⁷ Further, it sends a message that the community will eventually accept responsibility for remediation if industry does not.

2. Levy on industry

Revenue might also be raised through levies on industry. This option is frequently likened to the fund established to fund clean up of small oil spills. In Australia the fund was established by the Shipping Levy Act and the Shipping Levy Collection Act. Revenue is raised through a quarterly levy on the cargo capacity of ships, and collection is by Customs.⁷⁸ A similar model exists in New Zealand in the form of the Accident Compensation levies on industry which fund compensation for personal injury.⁷⁹

One option would be a levy on industries or industrial processes which, by their nature, are likely to cause significant contamination problems. The fund would then be used to fund orphan site clean up, including the clean up of future sites where cost of remediation exceeds the resources of the polluting company.⁸⁰ Revenue would therefore be raised by a mechanism which targets the riskiest industries, encouraging the implementation of higher safety standards in those industries, and internalisation of the associated costs.

This form of levy requires a new form of tax instrument, has high administrative costs, and has high compliance costs for the industries

⁷⁵ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, at 36.

⁷⁶ Australian Bankers' Association, *Position Paper: Banks and the Environment* (1992) 7; ANZECC, supra note 14, at 22.

⁷⁷ Iles, "Law and Change: Financial Liability for the Clean up of Contaminated Land" (1993) 19 *Melbourne University Law Review* 449, 462; Osmers, supra note 12, at 184.

⁷⁸ ANZECC, supra note 11, at 40.

⁷⁹ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, at 36.

⁸⁰ Osmers, supra note 12, at 184.

concerned.⁸¹ The ANZECC received little support for this option, the main support being from local government.⁸² Industry groups argued that the effect of such a levy would be “good environmental performers paying for the misdeeds of bad performers”, with potential inefficiencies and lack of effectiveness as a result.⁸³ Osmers, however, argues that this concern could be minimised by imposing the levy on a sliding scale, depending on the standards or level of protection desired. This would also “have the positive effect of raising the industry’s standards of management and operation”.⁸⁴

The second option for an industry levy is to impose a levy on chemicals and chemical products at their point of sale. This option targets those who benefit directly from the use of chemicals, whether industries or consumers.⁸⁵ The levy would be on a variable scale according to the level of risk associated with a particular chemical.⁸⁶ However, it does not provide an incentive to industry to improve standards of environmental performance.⁸⁷ The ANZECC suggested that this levy would be easily implemented.⁸⁸ However there may be high associated compliance costs which should also be considered.

A variant of this approach was presented in the New Zealand Ministry for the Environment discussion paper, where a unit charge on inputs or outputs of production is proposed. For example, a charge could be levied on chemical feedstocks, petroleum products, water or waste. However, administrative and compliance costs may be high where a new charge is involved, and revenue levels will be uncertain depending on factors such as efficiency of collection and possible substitutes for the product in the market.⁸⁹

Unsurprisingly, there is little support among industry for a levy on chemicals. Industry is generally in favour of the use of consolidated revenue to fund clean up.⁹⁰

⁸¹ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, at 36.

⁸² ANZECC, supra note 14, at 22.

⁸³ *Ibid*, at 14.

⁸⁴ Osmers, supra note 12, at 184.

⁸⁵ ANZECC, supra note 11, at 40.

⁸⁶ Osmers, supra note 12, at 184.

⁸⁷ *Ibid*, at 184.

⁸⁸ ANZECC, supra note 11, at 40.

⁸⁹ New Zealand Ministry for the Environment, *Discussion Document*, supra note 9, at 35.

⁹⁰ ANZECC, supra note 14, at 22.

A third option is for industry to establish a voluntary fund for orphan site remediation. This system is used in the Netherlands.⁹¹ In most of the old States in Germany, a combination of state financing and voluntary industry levies is used.⁹² However, this solution is resisted by industry in Australia and New Zealand. In Victoria, it has been consistently declined as it is seen as a mechanism whereby larger industries that are good environmental performers subsidise poorer performers.⁹³

3. Combination of collection mechanisms

The forms of revenue raising discussed are not mutually exclusive. Combinations of industry levies and funding from general taxes and rates are also possible.⁹⁴

For example, the Hazardous Substances Superfund in the United States is a congressionally established trust fund derived from a number of sources. Funds come from general appropriations, a special tax on petroleum and chemical products, an environmental tax on corporations, penalties and punitive damages from violators, costs recovered from responsible parties, and earned interest.⁹⁵ But the US superfund remains inadequate to meet the cost of remediation, so that the ultimate success of the remediation program relies on securing commitments from responsible parties.⁹⁶

Other options have also been suggested at various times, such as an environmental lottery or an environmental trust.⁹⁷ Although some efforts have been made to pursue these options, they are unlikely to offer a viable national solution to orphan site remediation.

B. Administering and Allocating Funds

A fund could be administered centrally by government or contracted out to the private sector. A stand-alone fund could take a number of corporate forms, such as trust, company, state-owned enterprise or quango. Any of these structures could be used to allocate funds, as full subsidies, flat rate or matching grants, or risk and cost-adjusted grants.

⁹¹ Osmers, *supra* note 12, at 184.

⁹² Reh binder, 'Contaminated Sites in Germany' in Rowe and Seidler, *supra* note 5, at 55.

⁹³ Osmers, *supra* note 12, at 184.

⁹⁴ New Zealand Ministry for the Environment, *Discussion Document*, *supra* note 9, at 36.

⁹⁵ Reh binder, *supra* note 92, at 58.

⁹⁶ Ludwiszewski, *supra* note 48, at 60.

⁹⁷ *Ibid*, at 58. ANZECC, *supra* note 11, at 41.

Any system of allocation should be equitable, transparent, and avoid capture by industry or remediation contractors.⁹⁸

VI. CONCLUSION

The urgent need for a national consistent approach to the problem of orphan site remediation is now clear. All that is now required is the political will to act. The ANZECC has produced useful recommendations on liability and the identification of orphan sites, which should be implemented by legislation. Once a consistent approach to liability is achieved, funds for remediation should be established by the Australian Commonwealth Government and by the New Zealand Government. Funding should be by a combination of industry levies and consolidated revenue, in accordance with the principles of equity and efficiency. Without such a national approach there seems little prospect that remediation will occur, and the risks to health and the environment will continue unabated.

⁹⁸ The US experience of overuse of private contractors and consequent abuses is documented by Latin, "Private Contractor (Mis)Use in the Superfund Program" in Rowe and Seidler, *supra* note 5, at 200-204.

GAINS FROM SHARE REALISATIONS: IS IT TIME FOR A LEGISLATED CAPITAL GAINS TAX?

BY BRETT WILKINSON AND STUART TOOLEY*

I. INTRODUCTION

Unlike many other advanced economies, New Zealand does not have an explicit capital gains taxation regime. The distinction between capital and income is therefore of vital significance.

An area in which the capital-income distinction is of considerable importance is that of gains and losses from the sale of shares. *Prima facie* such gains are of a capital nature and thus not taxable. However, depending on the circumstances, they may well come within the ambit of the income tax provisions. Essentially, gains on share realisation may be taxable where the gain constitutes a business profit, the taxpayer is dealing in shares, the taxpayer purchased the shares for the purpose of resale, or where the taxpayer is involved in a scheme or undertaking for the purpose of profit making.

The potential taxation of gains from share realisations is an issue of particular concern to investment companies. Recent case law would seem to indicate that the share acquisition and disposal activity of such companies might potentially be drawn into the income tax net. There remains, however, a considerable degree of uncertainty in respect of the issue and the Privy Council decision in *Rangatira*¹ has done nothing to clarify the general position of investment companies. The Inland Revenue Department's recent private ruling in respect of the TeNZ fund has further fuelled the existing uncertainty.

The current situation in respect of the taxability of gains from share realisations by investment companies serves as a useful illustration of the problems which arise by virtue of New Zealand having what may be described as an *ad hoc* approach to the taxation of capital gains. Clearly, uncertainty and the costs this imposes on the economy constitute one such problem. Additionally, the fact that some capital gains are taxed and some

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¹ *CIR v Rangatira* [1997] 1 NZLR 129.

are not introduces distortions in the behaviour of individuals and firms. This lack of a level playing field also results in the inequitable treatment of different forms of gains.

The appropriate solution, it would seem, would be to introduce a formal, comprehensive capital gains tax. In addition to redressing some of the problems noted above, such a tax would assist in realigning the judicial and economic definitions of income and restore some rationality to the use of income as a basis for imposing taxation.

This article reviews the tax implications of gains from share realisations. Particular attention is given to the position of investment companies. Part 2 discusses the capital-income distinction. Parts 3, 4 and 5 consider in some detail the statute and case law in respect of gains from share realisations. This discussion of the applied law is the central focus of the article.

Having ascertained the legal implications, part 6 reviews current issues and developments relating specifically to investment companies. Some attention is given to the TeNZ fund and the uncertainty that exists in the market regarding taxability of share realisation gains. Part 7 poses the question as to whether the observed problems in respect of investment funds suggest some need for a formal comprehensive capital gains tax. Part 8 provides concluding comments.

II. THE CAPITAL-INCOME DISTINCTION AND THE RATIONALE FOR TAXING "INCOME"

Like many developed economies, New Zealand makes use of income as a tax base. Tax systems commonly use income as a basis for taxation since it is considered to reflect *capacity to pay*. Income is merely:

a word used to refer to a subtle, complex concept. It is a manageable surrogate for a less concrete, more amorphous concept, ability to pay.²

Problems arise, however, since the tax law does not provide a comprehensive definition of income. It has thus been left largely to the judiciary to interpret the meaning of the term income, as has been the case in other jurisdictions adopting the income tax base.³

² Bittker, Stone & Klein, *Federal Income Taxation* (1984) 10, cited in Ross, S, and Burgess, P *Income tax: A critical analysis* (1991) 33.

³ Ross and Burgess, *supra* note 1.

There is, therefore, a strong incentive for an entity or individual receiving a gain to demonstrate that that gain does *not* constitute income as reflected in the wording of the statute law, but, instead, is of a capital nature.

Clearly, from an economic perspective, *all* gains comprise income *including* those of a capital nature. According to Simons, income:

is merely the result obtained by adding consumption during the period to 'wealth' at the end of the period and then subtracting 'wealth' at the beginning. The sine qua non of income is gain.⁴

This definition has not, however, been reflected in the approach adopted by the judiciary. Writing in respect of the Australian context, which is equally applicable to New Zealand, Parsons notes that the courts have relied on the definition of income as encapsulated in the law relating to trusts. He suggests that:

The concept of income as it was received from trust law could not be 'extended' to include capital gains, for it did not have a notion of income as a gain, or a notion of a capital gain. It knew only a distinction between a flow that belonged to the income beneficiary, and the proceeds of capital that belonged to the capital beneficiary.⁵

Thus, a considerable body of case law has developed which is based around the definition of income and the distinction between capital and income. To the extent that the merit of using income as a tax base depends on its role as a proxy for capacity to pay, this divergence between the economic and the judicial view of income is undesirable.

While gains from share sales would comprise economic income, they may not necessarily comprise judicial income. However, recent legal developments indicate a tendency for the two definitions to move toward greater alignment. Before focusing on the details of the case law, it is appropriate first to review the wording of the applicable statute law.

III. STATUTE LAW

Part C of the Income Tax Act 1994 outlines the items that are assessable for income tax. The items identified are, however, not exhaustive. Sections CD3

⁴ Cited in Parsons, "Income taxation - An institution in decay?" (1986) 3 *Australian Tax Forum* 233-266.

⁵ Parsons, *supra* note 3, at 235.

and CD4 are potentially applicable to profits arising from the sale of shares. These sections read:

CD3 ... any amount derived from any business.

CD4 ... any amount derived from the sale or other disposition of any personal property or any interest in personal property (not being property or any interest in property which consists of land), if the business of the taxpayer comprises dealing in such property, or if the property was acquired for the purpose of selling or otherwise disposing of it, and any amount derived from the carrying on or carrying out of any undertaking or scheme entered into or devised for the purpose of making a profit: ...

Under the Income Tax Act 1976, these sections pertained to 65(2)(a) and 65(2)(e), respectively.

CD3 essentially requires that the taxpayer be in business and that the profits arising be derived from a part of that business. CD4 contains three limbs, which may be applicable in the case of, profits arising from share sales. These are:

1. the taxpayer must be in the business of dealing in shares; or
2. the shares were acquired with the intention of resale; or
3. the purchase of the shares arises in the context of an undertaking or scheme for the purpose of profit making.

The distinction between CD3 and the first limb of CD4 is quite subtle. The *CCH New Zealand Master Tax Guide* notes:

In practice, any profit or gain assessable under [the first limb of CD4] will almost invariably be assessed as a business profit under s CD3.⁶

Whilst this could generally be regarded as being the case, it will not always be so. In *Piers & Ors v CIR*,⁷ the High Court found that the taxpayers were *not* in business and hence CD3 did not apply. However, the taxpayers were found to be dealing in shares and hence the profits were taxable by virtue of the first limb of CD4.

⁶ Commerce Clearing House *New Zealand Master Tax Guide* (1998) section 5-218.

⁷ (1995) 17 NZTC 12,283.

IV. PROFITS FROM BUSINESS - CD3

The situation as to when profits or gains from the sale of shares will constitute business profits is not immediately apparent. Some review of the extensive case law is required in order to clarify the meaning of the legislation.

The leading case in respect of this issue is that of *Californian Copper Syndicate (Limited and Reduced) v Harris (Surveyor of Taxes)*.⁸ In this case, the taxpayer acquired a copper-bearing property which it later sold for shares in the purchasing company. Clerk LJ commented that:

It is quite a well settled principle in dealing with questions of assessment of income tax, that where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income Tax Act of 1842 assessable to income tax. But it is equally well established that enhanced values obtained from realisation or conversion of securities may be so assessable, where what is done is not merely a realisation or change of investment, but *an act done in what is truly the carrying out of a business*.⁹ (emphasis added)

In this instance, it was found that the gain made on sale of the property did not arise from a realisation of the company's investment. Rather, the gain arose as part of the company's business operations. The company's articles of association gave the clear impression that acquisition of the property for resale at a profit was a part of the business. Lord Trayner noted:

This is not, in my opinion, the case of a company selling part of its property for a higher price than it had paid for it, and keeping that price as part of its capital, nor a case of a company merely changing the investment of its capital to pecuniary advantage. My reading of the Appellant Company's Articles of Association along with the other statements in the case satisfy me that the sale on which the advantage was gained, in respect of which income tax is said to be payable, was a proper trading transaction, one within the Company's power under their Articles, and contemplated as well as authorised by their Articles. I am satisfied that the Appellant Company was formed in order to acquire certain mineral fields or workings - not to work the same for themselves for the benefit of the Company, but solely with the view and purpose of reselling the same at a profit.¹⁰

⁸ (1904) 5 TC 159.

⁹ At 166.

¹⁰ At 167.

In essence, then, this case clearly established the view that a gain, which may generally be regarded as being of a capital nature, could actually be characterised as being of an income nature because of the circumstances in which the transaction took place. The gain came within the income provisions by virtue of it being a profit of the business. The difficulty, of course, is defining the circumstances in which a transaction will fall within the ambit of the income provisions. On this point Clerk LJ noted:

What is the line which separates the two classes of cases may be difficult to define, and each case must be considered according to its facts; the question to be determined being - Is the sum of gain that has been made a mere enhancement of value by realising a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?¹¹

It is not necessary that the taxpayer be carrying on a business *specifically* dealing in investments. The Privy Council in *Punjab Co-operative Bank Ltd v Commissioner of Income Tax*¹² articulated this principle in the following manner:

their Lordships do not wish to give any support to the contention that, in order to render taxable profits realised on sale of investments, in such a case as that before them, it is necessary to establish that the taxpayer has been carrying on what may be called a separate business either of buying or selling investments or of merely realising them.¹³

The same principle was outlined by Richardson J (as he then was) in *AA Finance Ltd v CIR*:¹⁴

Liability to tax does not depend on showing that the taxpayer is carrying on a separate business of dealing in investments. A transaction may be part of the ordinary business of the taxpayer or, short of that, an ordinary incident of the business activity of the taxpayer although not its main activity. A gain made in the ordinary course of carrying on the business is thus stamped with an income character.¹⁵

Having said that, it should also be noted that not all gains arising within a business context would constitute income gains. The High Court of

¹¹ At 166.

¹² [1940] AC 1,055.

¹³ At 1,072.

¹⁴ (1994) 16 NZTC 11,383.

¹⁵ At 11,391.

Australia noted this fact in *Colonial Mutual Life Assurance Society Ltd v FCT*¹⁶ and went on to state that:

the definition only refers to proceeds which would be held to be income in accordance with the ordinary usages and concepts of mankind, except so far as the Act states or indicates an intention that receipts which are not income in ordinary parlance are to be treated as income.¹⁷

Barwick CJ similarly noted in a dissenting judgment in *London Australia Investment Co Ltd v FCT*¹⁸ that:

Of course, what is produced by a business will in general be income. But whether it is or not must depend on the nature of the business, precisely defined, and the relationship of the source of the profit or gain to that business. Everything received by a taxpayer who conducts a business will not necessarily be income. As I have said, it must depend on the essential nature of his business and the relationship of the gain to that business and its conduct.¹⁹

Within the case law, a subset of cases has evolved dealing specifically with the situation of profits from share sales arising in the context of the banking and insurance industries. To an extent, it may be argued that the principles so determined are applicable only to the banking and insurance industries. However, this will not always be the case. In *London Australia*, it was argued on behalf of the taxpayer that the findings in respect of cases such as *Colonial Mutual Life Assurance*, *Punjab* and *Australasian Catholic Assurance Co Ltd v FCT*²⁰ were specific to the banking and insurance industries. In respect of this argument Gibbs J said:

With all respect I cannot agree. In all those decisions the test suggested in *Californian Copper Syndicate v Harris* was applied. That test is applicable to any business, and if the sale of the shares is an act done in what is truly the carrying on of an investment business the profits will be taxable just as they would have been if the business had been that of banking or insurance.²¹

It is possible, then, that the situation facing investment companies may be affected by the findings in the banking and insurance industry cases. They

¹⁶ (1946-47) 73 CLR 604.

¹⁷ At 615.

¹⁸ [1976-77] 138 CLR 106.

¹⁹ At 112.

²⁰ (1958-59) 100 CLR 502.

²¹ [1976-77] 138 CLR 118.

should not be discounted as being industry-specific. Some closer review of these cases is therefore appropriate.

It is of course necessary to bear in mind that statutory changes in New Zealand have had considerable implications for the situation faced by banks and insurance companies. Specifically, section CM10 renders life insurance companies liable for taxation on *all* profits or gains, while the accruals regime has implications for gains arising in the context of financial arrangements.

1. The banking and insurance cases

The common law relating to banks and insurance companies indicates that share realisations by such companies would generally be regarded as a normal part of business operations. Heron J in *State Insurance Office v CIR*²² provided a comprehensive review of the applicable banking and insurance cases, noting that:

the special circumstances of the business carried on by bankers and insurers have often required that the sale or realisation of investments be rendered income in the circumstances of those cases;²³

and:

The rationale behind the banking and insurance cases is the common business requirement of regular realisation of investments in order to conform to certain ratios or actuarial assessments thought necessary for the purposes of an insurance or banking business or otherwise to carry out the objects of the business.²⁴

The comments of the Privy Council in *Punjab* as regards the business of banking are of particular relevance and clearly enunciate the principle involved. It was stated that:

In the ordinary case of a bank, the business consists in its essence of dealing with money in credit. Numerous depositors place their money with the bank, often receiving a small rate of interest on it. A number of borrowers receive loans of a large part of these depositors' funds, at somewhat higher rates of interest. But the banker has always to keep enough cash or easily realisable securities to meet any probable demand by the depositors. No doubt there will generally be loans to

²² (1990) 12 NZTC 7,035.

²³ At 7,046.

²⁴ At 7,064.

persons of undoubted solvency which can quickly be called in, but it may be very undesirable to use this second line of defence. If, as in the present cases, some of the securities of the bank are realised in order to meet withdrawals by depositors, it seems that this is a normal step in carrying on the banking business, or in other words, that is an act done in 'what is truly the carrying on' of the banking business.²⁵

In *CIR v Auckland Savings Bank*,²⁶ North P similarly noted that:

it is a well stated principle in dealing with questions of income tax that where the owner of an ordinary investment chooses to realise it and obtains a greater price for it than he originally acquired it at, the enhanced price is not a profit assessable to income tax. But on the other hand it is equally well established that enhanced values obtained from realisation or conversion of securities may be so assessable when what is done is not merely a realisation or change of investment but an act done in what is truly the carrying on or carrying out of a business. This latter principle ... has been applied time and again to banks and other institutions such as life insurance companies which require to invest a substantial part of their funds in readily realisable gilt edged investments in order to meet in the case of banks the demands of their customers and in the case of life insurance companies the claims of policy holders.²⁷(emphasis added)

In respect of insurance companies, the High Court of Australia in *Colonial Mutual Life Assurance* referred to the similarity of insurance and banking business, stating that:

In our opinion there is no substantial distinction between the business of an insurance company and that of a bank in this respect.²⁸

In delivering the judgement of the Court, Williams J said:

But an insurance company ... is undoubtedly carrying on an insurance business and the investment of its funds is as much a part of that business as the collection of the premiums.²⁹

In *Australasian Catholic Assurance*, the taxpayer purchased blocks of flats as investments. The Commissioner assessed the taxpayer for tax on the

²⁵ [1940] AC 1,055, 1,072.

²⁶ [1971] NZLR 569.

²⁷ At 573.

²⁸ (1946-47) 73 CLR 604, 620.

²⁹ At 619.

profits earned from sales of several of the blocks of flats. Menzies J found that the profits made from sale of the flats arose from the carrying on of the taxpayer's business and thus were assessable. He stated:

That they were profits from the carrying on of that business is, I think, an inescapable conclusion. The flats were bought as good investments and sold to avoid their becoming bad investments, which was what was intended from the very first, although it was hoped, and indeed, expected that they would both have to be sold until a long time after 1951.³⁰

His Honour did, however, make it clear that his decision would not render taxable all profits from real estate sales, and presumably, by implication, from other investments, made by insurance companies. He noted:

It was said here that if the profit which the taxpayer made is taxable, so is every other profit made by a taxpayer when it sells part of its real estate; but my decision falls short of the acceptance of such a conclusion and rests upon the narrower ground that this taxpayer, as part of its ordinary investment business, bought real estate to obtain a high return and sold it profitably when it was found to be producing a low return, and so made a profit upon its buying and selling which I regard as income according to ordinary concepts, because in the ordinary course of carrying on business, the taxpayer must from time to time change its investments to use its funds to the best advantage.³¹

The courts have in fact *not* indicated that *all* gains from realisation of investments by banks and insurance companies are income. In the *State Insurance Office* case, the High Court of New Zealand found that certain share transactions did *not* comprise part of the business of the taxpayer. In this particular instance, the shares held were regarded as being a part of the taxpayer's fixed, rather than circulating, capital. This was essentially because the taxpayer was not considered to be likely to need to rely on this investment in order to meet its short-term liabilities. Heron J noted that:

In my view, the fact that shares have not been sold to meet claims is not just a matter of happy coincidence. It is not merely fortuitous that circulating capital has been sufficient to meet current liability.³²

It was, however, noted that the decision was unusual. Heron J noted:

³⁰ (1958-59) 100 CLR 502, 505.

³¹ At 509.

³² (1990) 12 NZTC 7,035, 7,040.

It will be seen from the conclusion I have reached that State's case is an unusual one brought about by quite unique considerations and as a result departing from the outcome of most of the banking and insurance cases.³³

Similarly, in the *National Bank of Australasia Ltd v FCT*,³⁴ the High Court held that certain share realisations did not constitute part of the business of the bank. In this case the bank had acquired shares in a pastoral company as a part of a merger with the Queensland National Bank. The shares had been acquired to enable the bank to gain the

benefit of being known to have moved into the same relationship with the pastoral company as the Queensland National Bank had maintained.³⁵

Realisations of these shares did not give rise to a business profit.

Perhaps the key point in the insurance and banking cases is whether the investments form part of the fixed or circulating capital. The Court of Appeal made reference to this issue in *CIR v Inglis*.³⁶ McKay J noted:

The concept of fixed and circulating capital is a helpful one. It recognises the distinction between what is invested in revenue producing assets of an ongoing nature, and what is invested in goods which are traded or which are manufactured and sold. The money invested in such assets circulates, in that it comes back to the business as cash as the assets are sold, and is reinvested similarly again and again. It is part of the working capital of the business, and is represented by the stock in trade. If a person was in the business of trading in shares, then his share portfolio would be his stock in trade, and his investment in shares would represent circulating capital.³⁷

In large part, it seems that investments by banks and insurance companies comprise circulating rather than fixed capital. The same issue is potentially applicable to investment companies.

2. *The investment company cases*

The investment company situation is of particular interest. Presently, there is some uncertainty surrounding the extent to which gains from share realisations by such companies constitute income.

³³ At 7,064.

³⁴ [1968-69] 118 CLR 529.

³⁵ At 536.

³⁶ (1992) 14 NZTC 9,180.

³⁷ At 9,189.

In *London Australia*, the High Court of Australia by a majority held that the realisation of shares at a profit constituted part of the business of the taxpayer. The company invested in Australian securities in order to obtain dividend income. The company had an investment policy of maintaining a consistent 4 percent yield on its capital. Gibbs J noted:

the taxpayer never bought shares for the purpose of profit making by sale, or with the intention of selling them, or simply because their market value was likely to increase. It bought shares to hold as an investment to yield dividends, but it foresaw that it was likely that the shares would increase in market value, and of course hoped that this would occur. If the shares did increase in value, but the dividend rate did not correspondingly increase, the dividend yield would fall, and the taxpayer would then be likely to sell the shares.³⁸

His Honour went on to find:

Although the company's business was to invest in shares with the primary purpose of obtaining income by way of dividends, the conduct of the investment business required that the share portfolio should be given regular consideration, and that the shares should frequently be sold when the dividend yield dropped, which for practical purposes usually meant when the shares went up in value. The taxpayer systematically sold its shares at a profit for the purpose of increasing the dividend yield of its investments. The sale of the shares was a normal operation in the course of carrying on the business of investing for profit. It was not a mere realisation or change of investment.³⁹

Similarly, Jacobs J stated:

But when with such an investment policy which envisages regular and frequent sales of the shares acquired, operations are conducted on such a very large scale, the proper conclusion is that the acquisitions and disposals of shares were part of a business of acquisition and disposal.⁴⁰

However, Barwick CJ, dissenting, stated that:

But, as the maintenance of the subscribed capital and of a consistent yield upon it was also of the essence of the company's business, realisation of shares from time to time became necessary or advisable ... Those realisations could be said, in my

38 [1976-77] 138 CLR 115.

39 At 117.

40 At 131.

opinion, to be a result of the nature of the company's business but not part of that nature.⁴¹

3. *The Rangatira case*⁴²

In New Zealand, the situation of an investment company realising shares was considered recently in respect of the position of Rangatira Ltd.

The taxpayer was an investment company that had made gains from share sales over the period 1983-90, which the Commissioner had assessed, for tax. The High Court found for the taxpayer, except in respect of a number of share transactions which were held to be taxable on the basis that the shares had been acquired for the purposes of resale.

The Commissioner appealed, but the taxpayer did not cross-appeal the finding that some of the profits were taxable. The Court of Appeal⁴³ suggested that the same criteria as applied in *London Australias* should also be applied in the current case. The Court dismissed the appeal in respect of the 1986 year, but upheld the appeal in respect of the years subsequent to 1986. It was held that:

at least from April 1985 Rangatira was selling shares as part of its ordinary business, or as an ordinary incident of its business. The sales were not merely a realisation or change of investment, but were done in what was truly the carrying on of a business.⁴⁴

It would appear that whilst the Court of Appeal accepted that many of the share realisations did not in their own right give rise to a taxable profit, the fact that some purchases were motivated by the purpose of resale tended to characterise the entire company as being in the business of share trading. The Court stated that:

The picture which emerges is not that of a passive investor. The sale of part of the share portfolio in order to acquire the interests of the other shareholders in the James Cook Hotel, and the further sales to enable the purchase of the freehold and the car parking building beneath the hotel, do not of themselves suggest that selling shares was an ordinary incident of the business. Nor does the acceptance of takeover offers. The sale of equities in order to balance the portfolio by including in it a substantial

⁴¹ At 113.

⁴² *Supra* note 1.

⁴³ (1995) 17 NZTC 12,182.

⁴⁴ At 12,191.

holding of Government stock is likewise neutral, when considered on its own. These transactions, however, form only part of a greater whole.

The sales of shares in the Brierley group to supplement income, and the TKM transactions, were held to be income within the second limb of s 65(2)(e). We think they would also fall within s 65(2)(a), as being 'acts done in what is truly the carrying on of a business', and as 'part of the ordinary business of the taxpayer'.

They were not identified as part of some separate and distinct business. They inevitably colour the other transactions, such as sales to fund the purchase of other shares, and the sales made to fund the major acquisitions in respect of the James Cook Hotel and the investment in Government stock.

As a prudent investor, Rangatira clearly reviewed its portfolio of investments and from time to time changed them. When one looks at the totality of the transactions, *it is difficult to resist the inference that in selling shares the company was seeking to enhance its position, not merely by achieving a balanced portfolio of income producing investments, but also by making gains from the sales themselves.*⁴⁵(emphasis added)

The taxpayer appealed to the Privy Council. It was initially hoped that the findings of the Privy Council would clarify the tax position of investment companies. However, while the Privy Council found in favour of the taxpayer, the decision appears to have little or no bearing on the general investment company position. Smith⁴⁶ summarises two major points to come out of its decision. First, whilst it was acknowledged that certain share transactions were subject to tax, overall the company had not changed its business emphasis. Second, the Privy Council held that the Court of Appeal could not overturn the decision of the High Court on a question of fact unless that decision was held to be wrong. The Privy Council concluded:

It seems clear that the number and frequency of the transactions during the seven years under review would not alone have persuaded the Court of Appeal to differ in their conclusion from that of Gallen J. It was the change of policy asserted by the respondent to have occurred ... which evidently led the Court of Appeal to conclude that the conclusion reached by Gallen J was erroneous. Yet this conclusion was based upon Mr Steele's evidence that the Brierley related transactions were exceptional, and did not reflect a change in the policy of the appellant or in the nature of its business as a whole. This was evidence, fully tested in cross

⁴⁵ At 12,190-12,191.

⁴⁶ Smith, "The Rangatira Decision" (1997) 76 (1) *Chartered Accountants Journal of New Zealand* 35.

examination, which Gallen J had heard and which the Court of Appeal had not ... It was for Gallen J to assess the reliability of Mr Steele as a witness. It does not follow of course that another judge hearing that evidence would have given it the same weight. Looking at the matter in retrospect their Lordships would think that the decision at first instance could have gone either way, but that is not to say that it was wrong. In their Lordships' view the decision of Gallen J was one which he was entitled to reach, and one which should not have been reversed.⁴⁷

As stated by Davies, it appears that:

the Law Lords based their long-awaited judgement more on a technicality ... than on a principle of tax law, thus disappointing those hoping to see a definitive line drawn between capital and revenue items.⁴⁸

The current position facing investment companies is discussed further in part 6 in this article.

4. *The Piers case*⁴⁹

A further recent case, which is relevant to the issue of whether a taxpayer is carrying on or carrying out a business, is that of *Piers*. The case related to the Alexander and Alexander Pension Plan, the investments of which were managed by Westpac Investment Management (NZ) Ltd. The Commissioner assessed the trustees for gains from share transactions on the basis that the transactions were part of the ordinary business of the taxpayers, that the shares were acquired for the purposes of resale, and that the taxpayers had entered into an undertaking or scheme for the purpose of making a profit.

The taxpayers appealed to the High Court and, while the Court held the transactions to be taxable, it was held that the taxpayers were *not* in business. Temm J stated in respect of the claim that the profits were business profits:

I can dispose of this argument quite briefly. The trustees were not in business at all. They had no customers, they were not trading in the ordinary business sense, and their sole purpose was to discharge the statutory and fiduciary obligations to act prudently in managing the fund.⁵⁰

⁴⁷ [1997] 1 NZLR 129, 139.

⁴⁸ Davies, "Law Lords find for Rangatira but leave capital gains in limbo" (December 6, 1996) *The Independent* 7.

⁴⁹ *Supra* note 7.

⁵⁰ (1995) 17 NZTC 12283, 12289.

His Honour differentiated between insurance companies and superannuation funds stating that:

While in both cases it can be said that the predominant consideration 'in acquiring securities is to obtain the best effective interest yield during the period of the date of acquisition and maturity', yet the reason for that consideration differs between the two kinds of entity - in the case of a superannuation fund it is to protect the value of the capital, but in the case of the life insurance company it is to enhance the profitability ... the two entities under discussion have quite different reasons for existence.⁵¹

The implications of such a finding for superannuation funds are significant. Of particular interest in the *Piers* case is that his Honour went on to find that:

the fund was dealing in shares within the meaning of s 65(2)(e) during the three years in question.⁵²

As noted earlier, this would seem to be a somewhat unusual outcome and it would be more common for profits caught by the first limb of CD4 [formerly section 65(2)(e), Income Tax Act 1976] and to also come within CD3. Further consideration of the limbs of CD4 is undertaken in the following section.

V. DEALING, RESALE AND PROFIT MAKING - THE THREE LIMBS OF CD4

CD4 applies to personal property. The Courts have accepted that shares constitute personal property for the purposes of this subsection. In *Inglis*, McKay J expressly stated that "Shares are personal property".⁵³ To that end, the three limbs of this section may operate to render taxable gains made from share realisations. Each of the three limbs are addressed in further detail below.

1. Dealing in shares

The first limb of CD4 renders taxable profits or gains from sale of property where the business of the taxpayer comprises dealing in such property.

⁵¹ At 12,290.

⁵² At 12,293.

⁵³ (1992) 14 NZTC 9,180, 9,188.

Reference has already been made to the fact that most gains coming within this limb will also come within CD3.

The findings of the High Court in *Piers* indicates that the volume of transactions that have taken place are of considerable importance in ascertaining whether the taxpayer is dealing in shares. Temm J noted that:

The frequency of share dealing is often decisive in deciding whether a taxpayer's profits are liable to assessment under s 65(2)(e). The purpose or motive for this kind of business enterprise is of less relevance than the extent of it ⁵⁴(emphasis added)

In dismissing the taxpayer's objection, his Honour went on to point out that, even though the taxpayer may not have intended to deal in shares, the evidence of the frequent transactions indicated that it was in fact so doing:

While evidence of a taxpayer's intentions as to financial transactions is admissible and relevant when deciding whether share dealings are covered by the first limb of s 65(2)(e), that is not decisive because the issue has to be decided objectively not subjectively. No doubt the trustees, as they said, did not wish to trade in shares, and no doubt also their intentions throughout were to meet their obligations to act prudently and to protect the fund from erosion. But Westpac's many share transactions made on the trustee's behalf lead me to the conclusion that the fund was dealing in shares within the meaning of s 65(2)(e).⁵⁵

Despite the High Court's comments, it would not be wise to attach too strong an emphasis to the volume of transactions *alone* as determining whether a taxpayer is dealing in shares. As indicated in *London Australia*, the volume provides an indication of the existence of a business but it is not necessarily the determinant. Hence, low volumes of share transactions may not necessarily prove a valid defence against a claim that the taxpayer is dealing in shares.

2. The intention of resale

The second limb of s CD4 provides that profits on share sales may be taxable where the property (in this case shares) was obtained for the purpose of resale. The key case in respect of this limb is *CIR v National Distributors*.⁵⁶ The case involved investment of excess capital by the taxpayer company in the sharemarket. The Court of Appeal found by a

⁵⁴ (1995) 17 NZTC 12,283, 12,292.

⁵⁵ At 12,293.

⁵⁶ (1989) 11 NZTC 6,346.

majority that the taxpayer had acquired the shares for resale. This was despite the taxpayer's *motive* being to invest in shares as a hedge against inflation.

Three particular points in respect of this limb warrant mention. The first relates to the fact that "purpose" refers to the taxpayer's *subjective* purpose. Richardson J stated:

It is well settled that the test of purpose is subjective requiring consideration of the state of mind of the purchaser as at the time of acquisition of the property.⁵⁷

This subjective test is opposed to the objective test in the first limb, as stated by Temm J in *Piers*.⁵⁸ However, whilst the emphasis is on the subjective purpose, Richardson J also noted:

Where subjective purposes are in issue the statements of the taxpayer, or of someone who can speak for the taxpayer, are obviously important evidence. But for obvious reasons they must be assessed and tested in the totality of circumstances which will include the nature of the asset, the vocation of the taxpayer, the circumstances of the purchase, the number of similar transactions, the length of time the property was held and the circumstances of the use and disposal of the asset. *Actions may speak louder than words and the totality of circumstances may negate the asserted purpose of the purchase.*⁵⁹

It is also relevant to consider that the:

inquiry under the second limb of sec 65(2)(e) is as to the purpose of the taxpayer at the time of acquisition. Whilst subsequent events may assist in ascertaining that purpose, they do not determine it.⁶⁰

The second point is related to the first and pertains to the onus of proof. Casey J, again in *National Distributors*, referred to *Williams Property Developments v CIR*,⁶¹ in stating that the onus of proof rests with the taxpayer. This was also reinforced by Quilliam J who went on to note that:

⁵⁷ At 6,350.

⁵⁸ (1995) 17 NZTC 12,283, 12,293.

⁵⁹ (1989) 11 NZTC 6,346, 6,351.

⁶⁰ At 6,358, per Doogue J.

⁶¹ (1980) 4 NZTC 61,537.

Unless the taxpayer can show that the main or dominant purpose which lead him or her to acquire the property was not to sell or otherwise dispose of it, then the profits or gains will be taxable.⁶²

However, it should be noted that the taxpayer is only required to show that the purchase was not with the intention of resale - the taxpayer does *not* need to demonstrate some alternative purpose.⁶³

The third point is that “purpose” refers to the *dominant* purpose of the taxpayer. That this is the case appears to be well accepted by the Commissioner (IRD, 1992). In *National Distributors*, Richardson J stated:

Where there is more than one purpose present taxability turns on whether the dominant purpose was one of sale or other disposition.⁶⁴

However, his Honour also stated that:

The analysis becomes more complicated where different purposes may be more significant depending on whether the focus is on the short term, the medium term or the ultimate objective.⁶⁵

As regards the determination of the dominant purpose, there may be a difference between motive and purpose. As noted above, the Court of Appeal in *National Distributors* held by a majority that the purpose of the taxpayer in acquiring the shares was resale, regardless of the motive. In this case, the taxpayer’s motive may have been to hedge against inflation - the purpose, however, was resale of the shares. In allowing the Commissioner’s appeal against the findings of the High Court, Richardson J (as he then was), referring to the decision of Quilliam J, stated:

he mixed purpose and motive: the purpose of resale and the motive of protecting capital in inflationary times through the management of a portfolio.⁶⁶

Casey J similarly noted:

It matters not that the purpose of buying shares to sell them later was arrived at in order to increase the taxpayer’s assets, or to provide a hedge against inflation. Those

⁶² (1989) 11 NZTC 6,346, 6,355.

⁶³ At 6,352, per Richardson J.

⁶⁴ At 6,350.

⁶⁵ At 6,350.

⁶⁶ At 6,353.

are merely the motives or wider objectives which give rise to the purposeful buying of shares for resale.⁶⁷

In a dissenting judgement, Doogue J stated that:

It is implicit in the language of the subsection, that the purpose of selling must be profit or gain for the dominant purpose of the taxpayer to be able to be ascertained. It is, I suggest, because no-one would naturally postulate a taxpayer purchasing property for the purpose of disposing of it by sale at any price, including a loss, that the Courts have so readily adopted the view that the inept language of the section can be read as if the method or activity by which the object or purpose is to be achieved, is itself the purpose.⁶⁸

In essence, it appears that the suggestion being made is that the legislature intended a tax impost where the purpose of the taxpayer is to make a profit, as opposed to the purpose being, as the section currently reads, to resell the property. In other words, it is suggested that the term “resale:” should be interpreted as “to make a profit through resale”. His Honour went on to conclude that:

The taxpayer’s purpose can be the avoidance of loss in the real value of the money available to the taxpayer by the purchase of an asset which is likely to hold its value in real terms. This is quite a different purpose from the purpose of seeking to achieve a return in excess of the rate of inflation, and quite another thing to acquire a property merely in the hope and expectation that the money used in its acquisition will not lose its real value as a result of the effect of inflation during the period for which the property is held.⁶⁹

The above comments would appear to be inconsistent with the advice of the Privy Council in *Holden v CIR*.⁷⁰ In that case, the taxpayer was entitled to receive some money in English pounds. His money was shifted to New Zealand by purchasing securities that were resold on the day of purchase, but for New Zealand currency. Although the Privy Council found for the taxpayer (by determining that no profit had been made), it was held that the purpose of acquisition was for resale. Lord Wilberforce said:

In the present case it is not relevant to enquire what was the dominant purpose, since the only purpose for which the securities were bought was that they should

⁶⁷ At 6,355.

⁶⁸ At 6,359-6,360.

⁶⁹ At 6,361.

⁷⁰ (1974) 1 NZTC 61,146.

immediately be sold. The appellants argued that this purpose was only incidental to the wider and more essential purpose ... namely to remit funds from the United Kingdom to New Zealand but that, in their Lordships opinion is irrelevant. There can only be one answer to the question for what purpose the securities were bought, and the fact that the purchases and sale were part of a wider objective cannot affect that answer.⁷¹

The findings of the majority in *National Distributors* with respect to motive and purpose seem to sit well with the Privy Council's judgement in the *Holden* case.

3. Undertaking or scheme for the purpose of making a profit

Professor Head described the Australian section, which was broadly equivalent to this limb, as a "subjective and uncertain test".⁷² Much the same could almost certainly be said of this limb.

The extent to which an undertaking or scheme must be of the character of a business deal, as suggested in the Australian case *McClelland v FCT*,⁷³ is unclear. The *CCH New Zealand Master Tax Guide*⁷⁴ asserts that this principle has been affirmed as good law in New Zealand. *Duff v CIR*⁷⁵ is cited in support of this assertion. However, Mancer and Veale refer to *Beetham v CIR*⁷⁶ and the views of Henry J as to the differences between the Australian and New Zealand laws. Mancer and Veale thus suggest that:

Accordingly, an undertaking or scheme may give rise to an assessable profit even though it is uncharacteristic of a normal business venture.⁷⁷

A useful summary of the requirements of the third limb can be found in the comments of Woodhouse P in *Duff*. Woodhouse P stated, referring to a forerunner to the third limb of CD4, that:

Quite correctly Mr Goddard analysed the third limb of that paragraph on the basis that there must be: (a) a profit or gain, and (b) the making, carrying on or carrying

⁷¹ At 62,147.

⁷² Head, "Capital gains taxation and business" in Collins, D J (ed), *Reform of business taxation* (1985) 72.

⁷³ [1971] 1 All ER 969.

⁷⁴ Supra note 6, at section 5-233.

⁷⁵ (1982) 5 NZTC 61,131.

⁷⁶ 3 ATR 342.

⁷⁷ Mancer, C J and Veale, J A *Staples' guide to New Zealand tax practice* (1998) 541.

out of an undertaking or profit making scheme, and (c) a nexus between that profit making scheme and the profit or gain that has been derived so that it can be said that it was 'derived from the carrying on or carrying out of' the undertaking or scheme.⁷⁸

Exactly what constitutes a scheme or undertaking is extremely difficult to ascertain. In fact, Gresson P in *CIR v Walker*⁷⁹ quoted the Court in *Australian Consolidated Press v Australian Newsprint Mills*⁸⁰ as saying that "'scheme' is a vague and elastic word".⁸¹

As noted by Mancer and Veal, the gain must be of an income nature and hence realisation of a capital asset does not come within the limb. In *Eunson v CIR*,⁸² land was acquired for the purposes of farming but later subdivided and sold. Henry J of the Supreme Court held that:

I cannot see by doing this he was carrying on or carrying out a scheme entered into or devised for the purpose of making a profit. He did not enter any scheme at all nor did he devise any scheme. He merely disposed of a surplus capital asset by eight separate sales instead of one sale of the whole.⁸³

A scheme was found to exist in *Duff*. In that case a timber merchant, a real estate agent and an engineering consultant entered a partnership to acquire land, subdivide and sell it. However, the Crown compulsorily acquired the land at some time after the land had been purchased. It was said on behalf of the taxpayers that the gain arose not from the carrying on or carrying out of the scheme but by way of frustration of the scheme. Woodhouse P stated:

there has never been any suggestion that the agreed compensation was based otherwise than upon a realistic valuation of the property ... although the resulting profit came to hand because the land was taken by the Crown it still was derived as the result of influences that had operated prior to the taking, at a time when the scheme had begun to operate, and so within the period during which the scheme was being carried on.⁸⁴

Barker J, also in *Duff*, arrived at the same conclusion, using different logic. His Honour said:

⁷⁸ (1982) 5 NZTC 61,131, 61,134.

⁷⁹ [1963] NZLR 339.

⁸⁰ [1960] 105 CLR 473, 479.

⁸¹ [1963] NZLR 339, 357.

⁸² [1963] NZLR 278.

⁸³ At 281.

⁸⁴ (1982) 5 NZTC 61,131, 61,134.

The intervention of the Education Department was a variation of the scheme with an earlier realisation of profit.⁸⁵

The issue at stake in *Piers* concerned the use by Westpac (the fund manager) of a computer-based statistical model in portfolio determination. The Commissioner asserted that the evidence indicated a scheme for profit-making. According to Temm J:

The scheme was said to be the Portfolio Optimisation Process mentioned earlier ... It is as plain as a pikestaff that Westpac operated a scheme of management. It was sophisticated, carefully supervised and strictly controlled. Its staff following the scheme had to be well informed, acutely aware of changes in the market place and in the changing fortunes of the trading companies in which shares were held ... But to say this was a scheme 'entered into or devised for the purpose of making a profit' is to enter another dimension altogether.⁸⁶

His Honour accordingly found that the profits derived on share realisations were not subject to tax by virtue of this limb.

It should also be noted that 'purpose', under the second limb, appears to refer to the dominant purpose. However, there is some dispute regarding this matter, as noted by Temm J in *Piers*:

I mention counsel carefully pointed out there is a divergence of opinion as to whether the purpose must be the '*predominant* purpose' or the '*sole* purpose' but as it turns out I need not decide that refinement.⁸⁷ (emphasis added)

Whether a single transaction can be broken into sub-components with different purposes applying to each is of interest. In *Walker*, the taxpayer bought 63 acres of land. His intention was to subdivide and sell 3 acres that were within the City of Invercargill, and add the remaining 60 to his adjoining farm. The Court of Appeal, by a majority, found in favour of the taxpayer. In considering whether the transaction came within the ambit of the third limb, Turner J said:

It may indeed be contended that the transaction amounted to a scheme entered into by the respondent for the purpose of making a profit. This submission, in my opinion must fail ... It may indeed be contended that the transactions, examined as without doubt they must be at the moment of original purchase, could be said to amount to a

⁸⁵ At 61,144.

⁸⁶ (1995) 17 NZTC 12,283, 12,291.

⁸⁷ At 12,291.

'scheme' whose essence was that the respondent, in purchasing the land as a whole, *intended or contemplated* the sale of the city sections to advantage, thereby securing the country land at a cheap net price. But, as has already been held, the fact that the respondent hoped or intended (incidentally) to sell the city sections to advantage is not compulsive to the conclusion that his *purpose*, or his dominant purpose, in entering into the transaction was to make a profit.⁸⁸

In a dissenting judgement, Gresson P suggested that it was possible to consider the purpose in respect of the 3 acres as distinct from the purpose in respect of the other 60 acres. His Honour stated:

It was manifest on the evidence that the respondent's intentions in regard to the road frontage land were quite different from those regarding the sixty acres of farming land; it is relevant to ascertainment of purpose the actual use which he proposed to make of the land in question. His purpose in regard to the farm land was entirely different from that in regard to the frontage land which from the time of its acquisition he intended to sell in sections.⁸⁹

While the comments of Gresson P above relate more to the second limb, they are of interest in making the point as to different purposes attaching to a single transaction, as opposed to the majority view that there was only one overall dominant purpose.

VI. INVESTMENT COMPANIES - CURRENT TAX STATUS AND DEVELOPMENTS

Having considered some of the relevant case law relating to the possible taxation of gains from share realisations, it is appropriate to pause and reflect on the current situation with respect to investment companies.

Following the Court of Appeal's decision in respect of Rangatira Ltd, it was perceived that many investment companies would become liable to tax on gains on share realisations. Trigg suggested that:

It would be a bold trustee or manager who refused to recognise a potential tax liability when dealing in equities.⁹⁰

According to Macalister:

⁸⁸ [1963] NZLR 339, 367.

⁸⁹ At 354.

⁹⁰ Trigg, "Financial investments: Tax implications" (1996) 75(8) *Chartered Accountants Journal of New Zealand* 14.

the industry has been gradually increasing its provision for tax from low levels, or in some cases none at all, through to full provisioning.⁹¹

A further response within the industry to developments in this area of potential tax liability was the emergence of the somewhat controversial TeNZ passive investment fund with its IRD approved tax exempt status:

TeNZ is a passive investment fund, which will hold a portfolio of securities of the 10-largest listed companies in the same weighting as the NZSE10 index.⁹²

TeNZ obtained a private ruling from the IRD that exempts any gains on share realisation by the fund from tax. Gaynor quotes the ruling as stating:

that any gains realised from the sale of shares by the fund, in order to match the composition and weighting of the index or to fund a redemption of units, will not be taxable to the fund.⁹³

Referring to the reason for the ruling, Trigg suggests:

the argument - and presumably that put up for the private ruling - was that shares were not acquired for the purpose of selling at a profit, but solely because of the need to maintain all of their securities within the NZSE10.⁹⁴

The implication appears to be that gains on share realisations by passive investment funds will not be drawn into the tax net. This apparent tax benefit appears to be encouraging similar funds.⁹⁵ Whether this is a beneficial move in terms of the broader economy is outside the scope of this article. The comments of Gaynor, however, warrant some mention. He asserts that:

From a general economic point of view, resources controlled under a passive fund structure are not reallocated quickly to their most effective use. Consequently a wholesale switch to passive fund management would not benefit the economy.⁹⁶

91 Macalister, "TeNZ muddies future for managed funds" (1996, July 5) *National Business Review* 64.

92 Gaynor, "TeNZ tilts the playing field and splits investment community" (1996, May 24) *National Business Review* 61.

93 Ibid.

94 Supra note 90, at 14.

95 Macalister, supra note 91, at 3.

96 Supra, note 92.

It certainly would appear that the potential exists for greater than optimal levels of investment monies to be directed into passive funds by virtue of the tax advantage.

The Privy Council's decision in favour of Rangatira Ltd appears to have changed little in respect of the tax position of investment companies. Whilst it was hoped that the decision would bring some certainty, the opposite would appear to be the case. Initial media reports evidenced some uncertainty amongst tax professionals in respect of the meaning of the decision.

The *New Zealand Herald* quoted Coopers and Lybrand tax partner John Shewan as saying "This is not the landmark decision people were hoping for".⁹⁷ Hunt, of the *National Business Review*; reported Mike Lennard, the Inland Revenue Department's head of litigation, as saying:

It neither clips the wings [of Inland Revenue] nor extends its powers. They [the law lords] have not accepted the conclusions put by either side in the way the law should be developed, neither have they laid down any general principles.⁹⁸

In contrast, Greg Cole, Deloitte Touche Tohmatsu tax practice national director, was reported as saying:

The decision represents a major setback for the Inland Revenue Department ... Effectively, the court has sent a very clear message that the only way that IRD will be able to tax capital gains is if it can convince the government to change the tax law.⁹⁹

Smith also infers that the case represented a setback for the Department:

The decision shows the stubborn attitude of the Department, and its willingness to take taxpayers to court in cases which perhaps should not have been selected in the first place if it had looked at them in an objective light.¹⁰⁰

A key point to note is the comment that "their Lordships would think that the decision at first instance *could have gone either way*".¹⁰¹ In essence, it

⁹⁷ "Tax law seen as no clearer" (December 4, 1996) *New Zealand Herald* A5.

⁹⁸ Hunt, "Privy Council shies away from change" (December 6, 1996) *National Business Review* 23.

⁹⁹ *Ibid.*

¹⁰⁰ Smith, *supra* note 46, at 36.

¹⁰¹ [1997] 1 NZLR 129, 139.

would seem that the Privy Council, whilst supporting the right of Gallen J to find as he did, was not endorsing his findings as such. The implication is therefore that other investment companies would be unwise to rely too heavily on the findings of the High Court in respect of Rangatira Ltd.

Perhaps the most apt comments are those of David McLay, the lawyer acting for Rangatira, as quoted in the *National Business Review*:

People had high expectations for their clients but this was not a case brought on behalf of the managed funds industry. This was Rangatira's case.¹⁰²

Clearly, then, there remains considerable uncertainty in respect of the tax position of investment companies. The exact manner in which the *de facto* capital gains tax applies to investment companies remains a mystery, albeit a costly one in terms of impact on the broader economy.

VII. IS IT TIME FOR A FORMAL CAPITAL GAINS TAX?

It is not the purpose of this article to review comprehensively the arguments for and against capital gains taxation. However, the area of gains on share realisations is one that raises several interesting and relevant points in respect of the existing capital-income distinction.

The discussion so far has demonstrated that gains from share sales, which may otherwise be regarded as being of a capital nature, may in fact be included as income by virtue of CD3 and CD4. These sections may be viewed as widening the income tax net to introduce, in effect, a form of capital gains tax. Casey J stated in *National Distributors*:

That provision brings within the meaning of 'assessable income' profits or gains which in the ordinary commercial understanding would be regarded as accretions to capital. What Parliament has done by it is to impose a limited form of capital gains tax.¹⁰³

Similarly, Richardson J stated:

Section 65(2) is expressed as a deeming provision. The assessable income of the taxpayer is deemed to include profits derived from transactions coming within the respective limbs of para (e).¹⁰⁴

¹⁰² Hunt, *supra* note 98, 27.

¹⁰³ (1989) 11 NZTC 6,346, 6,355.

¹⁰⁴ At 6,350.

This raises the issue as to the appropriate definition of income. In essence, as noted in part 1, income is used as a tax base by virtue of the fact that it proxies capacity to pay. The economist's version of income, reflecting capacity to pay, would include capital gains - it is only the fact that the courts have traditionally relied on the definition of income encapsulated in trust law that capital gains have escaped the income tax net.

While the legislation has gone some way toward including gains which would otherwise be considered to be of a capital nature in the income definition, this partial inclusion and the uncertainty associated with it have given rise to inequity and inefficiency. In respect of equity, Krever and Brooks have gone so far as to suggest that:

Considerations of fundamental fairness provide the main rationale for taxing capital gains. These considerations embrace both of the traditional tax equity criteria: horizontal equity, the need for equal treatment of persons with comparable abilities to pay; and vertical equity, the need for appropriate differences in the tax treatment of persons with different taxable capacities.¹⁰⁵

The fact that two investment companies, one active and one passive, can derive the same level of gain from share realisations and potentially pay different amounts of tax should be of concern to policy makers. It would seem to be the case that taxpayers with equivalent "economic" incomes may pay different taxes by virtue of the judicial interpretation of "income" and "capital".

The absence of a level playing field in the capital gains tax arena also has adverse efficiency effects. Some reference to the distortions associated with undue focusing of resources in passive funds was made in part 6 above. Krever and Brooks make some valid points. They argue:

The economic efficiency case for taxing capital gains rests on the most fundamental proposition underlying a market economy: in order to ensure the efficient allocation of resources and to spur economic growth, capital should be encouraged to seek its highest rate of return. If capital gains are not taxed, capital will flow to those assets and sectors in the economy in which tax-free capital gains can be realised and away from investments with a higher rate of return. Such distortions interfere with the efficiency of the economy and thus lower living standards and reduce potential for economic growth. The resulting economic distortions reduce New Zealand's international competitiveness at a time when its major trading partners are minimising the tax distinctions between income and capital gains, thereby

¹⁰⁵ Krever, R and Brooks, N *A capital gains tax for New Zealand* (1990) 43.

encouraging the most economically efficient allocation of capital in their economies.¹⁰⁶

As has been noted already, the existing provisions introduce a considerable degree of uncertainty in respect of certain situations. Referring to the *Rangatira* appeal to the Privy Council, Haas suggested that:

At issue is whether the council's ruling will remove uncertainty over the taxation of capital gains when buying and selling shares.¹⁰⁷

Unfortunately, it has not done so. Some practical evidence of the impact of this uncertainty can be seen in the comments of Gaynor, who points out that the:

Bank of New Zealand was so convinced that all funds were taxable last year it closed down passive fund BNZ Blue Chip Equity Trust following advice from tax experts.¹⁰⁸

There can be little doubt that this uncertainty is imposing an unnecessary cost on the New Zealand economy.

As Mersi and Eady suggest, "in practice the treatment of equity gains may never become certain until legislative changes are made".¹⁰⁹ The rationality of New Zealand's partial approach must surely now be questioned by policy makers and some consideration must be given to a comprehensive legislated approach. The political costs of introducing a formal capital gains tax need to be weighed against the economic costs of the current approach.

While a legislated capital gains tax cannot be expected to eliminate all uncertainty - and certainly the experience of other countries such as Australia would suggest otherwise - it can be expected to introduce a more consistent approach than that which has emerged within the context of the existing law. Moreover, it can be expected to enhance the operation of the income tax system itself by more closely aligning the concept of judicial income with that of economic income - the very notion on which income as a tax base is founded.

¹⁰⁶ Ibid, 61.

¹⁰⁷ Haas, "Rangatira TeNZ twist" (1996) *Financial Alert* 15.

¹⁰⁸ Gaynor, *supra* note 92, at 61.

¹⁰⁹ Mersi and Eady, "Rangatira - Privy Council reserves decision" (1996, August) *Tax briefing* 2.

VIII. CONCLUSIONS

This article has considered the tax implications of profits made from share realisations. New Zealand does not have a formal capital gains tax, so it is of vital importance whether or not such gains from realisation are brought within the income tax net by virtue of either CD3 or CD4. To some extent, the operation of these sections may be regarded as being a limited form of capital gains taxation.

The issue has become of particular importance to investment companies, and, as the article highlighted, there continues to be uncertainty in respect of this issue. The Privy Council *Rangatira* decision has not assisted in redressing this uncertainty.

What is clear from a review of the case law relating to gains from share realisations, is that there are fundamental problems with New Zealand's limited and somewhat *ad hoc* approach to taxing what may generally be regarded as capital gains. Not only is there significant and costly uncertainty, but the fact that some gains are tax free and others are taxed gives rise to distortions in the economy as well as substantial inequities.

While the article has not sought to review comprehensively the arguments for and against capital gains taxation, it has demonstrated that there are features of the current system which suggest a need for reconsideration of New Zealand's policy stance in respect of capital gains. A comprehensive capital gains tax would go some way to redressing the divergence between the income definitions of economists and the courts. In doing so, it may alleviate some of the problems of the current *ad hoc* approach, problems that are clearly demonstrated in the case of gains from share realisations.

LORD BROWNE-WILKINSON'S "IDENTIFIABLE TRUST PROPERTY" PRINCIPLE

BY RUTH WILSON*

I. INTRODUCTION

In *Westdeutsche Landesbank Girozentrale v Islington Borough Council*,¹ Lord Browne-Wilkinson, before embarking on a detailed examination of the plaintiff Bank's arguments, conveniently identified "[t]he relevant principles of trust law". These principles, described by His Lordship as "uncontroversial", "basic" and "propositions fundamental to the law of trusts", apply to express, implied and constructive trusts alike. They can be summarised as follows:

- (i) equity operates on the conscience of the owner of the legal interest;
- (ii) the owner of the legal interest cannot be a trustee of the trust property until aware of the facts alleged to affect his conscience;
- (iii) in order to establish a trust there must be identifiable trust property (unless dishonest assistance is involved).²
- (iv) once the trust is established, a trust beneficiary has an equitable proprietary interest in the trust property enforceable against subsequent holders other than the bona fide purchaser of the legal interest.

While considerable academic interest has been excited by the second principle, which appears to make an addition to the traditionally accepted requirements for a trust to arise, this article will examine the third principle (and incidentally suggest that the second principle forms part of the third principle correctly understood). It will focus on the words "identifiable trust property" to ascertain what His Lordship meant by this phrase.

The need to establish the exact meaning of these words arises from the fact that "identifiable" is used in more than one sense in the law of trusts and there are passages in His Lordship's judgment in which it is not readily apparent which usage he has in mind. Accordingly, part II of this article

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¹ [1996] 2 All ER 961, 988.

² In full the principle reads: "In order to establish a trust there must be identifiable trust property. The only apparent exception to this rule is a constructive trust imposed on a person who dishonestly assists in a breach of trust who may come under fiduciary duties even if he does not receive identifiable trust property"(at 988).

outlines the different usages of “identifiable”, along with two other matters³ which similarly provide a background context to His Lordship’s formulation of his third principle. This will be followed in part III by a summary of the facts in *Westdeutsche* and an analysis of Lord Browne-Wilkinson’s application of the third principle in his judgment. It will be suggested that Lord Browne-Wilkinson’s identifiable trust property principle goes beyond simply requiring “defined” property or semantic certainty of subject matter to establish a trust, and focuses on the issue of the proper constitution of trusts. Part IV will discuss the mechanics of identifying property so as to constitute the trust. A parallel will be drawn between identification necessary to transfer equitable title and ascertainment necessary to transfer legal property in sale of goods cases. It will be suggested that in some cases identification requires appropriation.

It should be noted that Gallen J in *MacIntosh v Fortex Group Ltd*⁴ specifically adopted and applied His Lordship’s third principle but no reference was made to it on appeal. The joint judgment of the Court of Appeal in that case did require “a separately identifiable fund” as a prerequisite of an institutional constructive trust.⁵

II. THREE BACKGROUND MATTERS

A. *The Role of Property within the Concept of a Trust*

In a passage in *Westdeutsche*⁶ that will be analysed in further detail below, His Lordship was at pains to point out that property is the only proper subject matter of a trust and that “[a] trust can only arise where there is *defined* trust property”. (emphasis added)

As Professor Hayton puts it:

At the core of the trust concept is a duty of confidence imposed upon a trustee *in respect of particular property* and positively enforceable in a Court of Equity by a person.⁷ (emphasis added)

³ Namely, the role of property within the trust concept and the need for the proper establishment of a trust.

⁴ (1997) 6 NZBLC 102,141, 102,146.

⁵ *Fortex Group Ltd (in receivership and liquidation) v MacIntosh* [1998] 3 NZLR 171. See case note at p 127 of this Review.

⁶ [1996] 2 All ER 961, 991.

⁷ Hayton, “The Irreducible Core Content of Trusteeship” in Oakley, A (ed) *Trends in Contemporary Trust Law* (1996) 47.

According to Oakley, the inherent nature of a trust is a relationship in respect of property, under which one person, known as a trustee, is obliged to deal with property vested in him for the benefit of another person, known as a beneficiary.⁸ Ford and Lee define a trust as an obligation enforceable in equity which rests on a person (the trustee) as owner of some *specific property* (the trust property) to deal with that property for the benefit of another person (the beneficiary) or for the advancement of certain purposes.⁹

Clearly then, property in the form of “defined”, “specified” or “particular” property is an essential ingredient of a trust. However, it is not a sufficient ingredient. Before a trust can arise, the property that is to be its subject matter must be linked with the trustee via a binding trust obligation. When the property is so linked it is described as being “impressed” with the trust, and the trust can then be said to be established or completely constituted.

B. The Need for a Trust to be Properly Established or Constituted

The focus on the meaning of “identifiable trust property” should not obscure the fact that, in formulating his third principle, His Lordship was considering what was necessary “in order to establish a trust”. His fourth principle also opens with a reference to the establishment of a trust.

There are two methods of establishing an express *inter vivos* trust. The settlor can make a declaration of trust in respect of the property (in which case she will remain the legal owner of the property and hold it on trust for the beneficiaries). Alternatively, the settlor can relinquish all interest in the property by conveying it to trustees and declaring the trusts on which it is to be held (in which case the trustees will become the legal owners of the property and hold it on trust for the beneficiaries). Whichever method is used, the declaration must refer to specific, particular or, to adopt Lord Browne-Wilkinson’s terminology, “defined” property and, to be enforceable, must comply with any applicable formality requirements of section 49 A of the Property Law Act 1952. Once that property is impressed with the trust obligation it becomes trust property, and the trust is spoken of as being “properly” or “completely” constituted. It is “a complete and perfect trust”.¹⁰

⁸ Oakley, *A Constructive Trusts* (3rd ed, 1997) 2.

⁹ Ford, H and Lee, W *Principles of the Law of Trusts* (3rd ed, 1996) 1000.

¹⁰ *Infra* note 19, and accompanying text.

The necessity for, and mechanics of, impressing property with the trust obligation in order to establish a valid express trust are well understood and fully set out in *Foreman v Hazard*:

Property may be impressed with an express trust in one of two ways: either by declaration of trust which involves a change in equitable ownership but not in legal title, or by a transfer of property to be held in trust by the transferee which involves a change in legal title and usually too in equitable ownership. No particular form of words is required but in whatever way the intention is expressed the three certainties must be satisfied: certainty of intention to create a trust - that a trust is definitely intended; certainty of the subject matter of the trust - that specified property is to be bound by the trust and certainty of objects, that is of the persons intended to have the benefit of the trust. In addition, the object of the trust must be lawful and any formalities required by law for constituting the trust must have been complied with.¹¹

While it can be seen from the above that the mechanics of “establishing” an express trust are explicit, straightforward and well understood, the same cannot be said in relation to the other two types of trust. It is not usual to speak of “establishing” an implied or constructive trust. Despite this it is nonetheless clear that, when Lord Browne-Wilkinson referred to “establishing” a trust in his third principle, he definitely had constructive trusts in mind.¹² His first and second principles refer specifically to express, implied (resulting) and constructive trusts and it is reasonable to assume that the remaining principles stated in terms of “a trust” are intended to apply to all types of trust equally.

To discover what Lord Browne-Wilkinson had in mind when he spoke of establishing a trust, particularly in relation to constructive trusts, it is helpful to consider Oakley’s basic definition of the three types of trust:

An “express” trust is said to arise where the settlor expressly creates a relationship of trustee and beneficiary; a “resulting” trust is said to arise where the settlor carries out some other transaction from which the court infers a relationship of trustee and beneficiary; and ...a “constructive” trust is said to arise where the court imposes upon certain persons a relationship of trustee and beneficiary. In other words, an express trust arises out of the intentional creation of the relationship, a resulting trust arises out of some other intentional act of the settlor and a constructive trust arises totally independently of the intention of anyone.¹³

¹¹ [1984] 1 NZLR 586, 594.

¹² *Supra* note 2.

¹³ Oakley, *supra* note 8, at 29.

Replacing Oakley's notion of a trust "arising" with that of Lord Browne-Wilkinson's notion of a trust being "established", it is clear that whereas express and resulting trusts are established by the intentional¹⁴ act of the settlor, constructive trusts are established or imposed by the court in response to the constructive trustee's conduct. As Oakley puts it:

Constructive trusts arise by operation of law. Unlike all other trusts, a constructive trust is imposed by the court as a result of the conduct of the trustee and therefore arises quite independently of the intention of any of the parties.¹⁵

The conduct which triggers the imposition of the constructive trust has to be unconscionable. However, the relevant conduct does not exist in a vacuum. It is unconscionable conduct in relation to specific property that gives rise to an institutional, as opposed to a remedial, constructive trust.¹⁶

As Oakley points out, although most constructive trusts are imposed because of the circumstances in which the property that forms the subject matter of the trust has been acquired, there are cases in which the relevant conduct occurs after the property has been acquired.¹⁷ In both types of case it is the combination of specific property with conduct in relation to that property which provides the basis for the imposition of a constructive trust.¹⁸ It seems therefore that in the case of the constructive trust the unconscionable conduct performs the same function as the declaration of trust or the

¹⁴ In *Foreman v Hazard* [1984] 1 NZLR 586, 594, the court is speaking in terms of "the intention" to impress property with an express trust. The intention in such trusts takes the concrete form of a declaration of trust.

¹⁵ Oakley, *supra* note 8, at 1.

¹⁶ As to the difference between the two types of constructive trust: "A remedial constructive trust is one which is imposed by the Court as a remedy in circumstances where, before the order of the Court, no trust of any kind existed. The difference between the two types of constructive trust, institutional and remedial, is that an institutional constructive trust arises upon the happening of the events which bring it into being. Its existence is not dependent on any order of the Court. Such order simply recognises that it came into being at the earlier time and provides for its implementation in whatever way is appropriate. A remedial constructive trust depends for its very existence on the order of the Court; such order being creative rather than simply confirmatory" (*supra* note 8).

¹⁷ *Ibid.*, 5. While *Westdeutsche* was not of the former type of case, it would potentially have been of the latter type had the property in question not ceased to exist before the local authority had sufficient knowledge to do anything unconscionable in relation to it.

¹⁸ Note too that, unless the court orders otherwise, a constructive trust takes effect from the time of the relevant conduct (*Re Sharpe (a Bankrupt)* [1980] 1 WLR 219).

conveyance on trust does in the case of the express trust - the conduct links property with obligation. The conduct, in concert with the court order to which it leads, has the effect of impressing the property with the constructive trust. The trust is established or constituted at the date of the unconscionable conduct.

Support for the above explanation of the role of unconscionable conduct in establishing or constituting a constructive trust can be found in *Pooley v Budd*:

Trusts, however may be constituted not merely by direct declaration of trust, but also by constructive operation of the consequence flowing from the acts of the person themselves. Thus, equity will not merely enforce the execution of a trust against the trustees themselves but against all persons who obtain possession of the property affected by the trust, provided they had notice of the trust.¹⁹

In passing, it can now be suggested that if, as will be argued below, Lord Browne-Wilkinson by requiring “identifiable trust property” to establish a trust was requiring *defined property to be impressed with the trust obligation*, his separate second principle, that the holder of the legal interest must have knowledge of the facts alleged to affect his conscience to be a trustee, is superfluous as far as the constructive trustee is concerned. This is because a constructive trust is not “established” or (to use more appropriate language given that we are dealing with a constructive trust rather than an express or resulting trust), cannot be “imposed”, in the absence of unconscionable behaviour. Unless the would-be constructive trustee has knowledge of the facts which are alleged to affect her conscience, her behaviour in relation to the property cannot be “unconscionable” and no trust is established or imposed. Accordingly, as far as the constructive trust is concerned, it could be argued that there is no separate requirement for knowledge over and above what is already required by the third principle.

Similar points apply to the express trust. If the express trust is established by a declaration of trust it goes without saying that knowledge is present as a settlor cannot make a declaration of trust without being “aware that he is intended to hold the property for the benefit of others”. His declaration is in effect a statement of his intention, as from that date, now to hold property that he had previously owned absolutely for the benefit of others. If the express trust is established by the transfer of property in trust the trustee is again inevitably “aware that he is intended to hold the property for the benefit of others”.

¹⁹ (1851) 14 Beav 34.

Leaving aside further discussion of the role of knowledge in the resulting trust to others, it is suggested that, if the third principle is understood as suggested above, the second principle is superfluous in relation to express and institutional constructive trusts.

C. "Identifiability" arises in Two Distinct Aspects of Trust Law

1. Identifiability in the context of the certainty of subject matter requirement

The need for "specified", "particular" or "defined" property for a trust to exist has been referred to above in the context of the role of property in the trust. This requirement for the establishment of a valid trust is traditionally referred to as "certainty of subject matter".²⁰

The classic certainty case arose in situations where the would-be settlor failed either:

- (a) adequately to define, specify or describe the property which she intended to impress with a trust so that either the amount or the nature of the property available for the trust was vague or unclear (for example, "the bulk of my estate" or "my blue chip securities"); or
- (b) clearly to specify the share that each beneficiary was to receive.

The problem in such cases is purely semantic and arises from the use of relative words having no specific core of meaning.

However, as time went by, cases arose where the problem was not whether the property alleged to form the subject matter of the trust was described with sufficient semantic specificity, but whether property so described had been sufficiently *identified* for equitable title to pass. The issue typically arose in sale of goods cases where the vendor's insolvency supervened after payment and prior to delivery, making it crucial to determine whether title had passed to the purchaser. The Sale of Goods Act 1908 contemplates two types of goods: specific and unascertained. Specific goods pose no identification problems as by definition they are "goods identified and agreed on at the time a contract of sale is made".²¹ Property in specific goods passes when intended to pass.²² On the other hand, no property passes

²⁰ See *Foreman v Hazard* [1984] 1 NZLR 586.

²¹ Section 2.

²² Section 19.

in unascertained goods²³ “unless and until the goods are ascertained,” usually by appropriation to the contract.²⁴ Accordingly, in cases where the lack of appropriation prevented the passing of *legal* title under the Act, it has been argued that *equitable* title has passed so that the insolvent seller held the goods on trust for the purchaser. In what appears to be the first of these cases, *Re London Wine Company (Shippers) Ltd*,²⁵ decided in 1975 but not reported until 1986, Oliver J held that “...any such trust must fail on the ground of uncertainty of subject-matter”.²⁶ However, in the context of that case, involving a specified number of cases of a particular wine which had not been segregated from the dealer’s stock or in any other way appropriated to the contract, when Oliver J said, “to create a trust it must be possible to ascertain with certainty not only what the interest of the beneficiary is to be but to what property it is to attach”, it was identifiability that he had in mind rather than semantic uncertainty. The alleged trust lacked subject matter as it was impossible to tell which of the cases in the dealer’s hands were “trust property” and which were not.

When similar issues arose in *Re Goldcorp Exchange Ltd*,²⁷ the trust argument was again rejected by the Privy Council, and it was held that the same reasons which prevent passing of legal title in unascertained goods apply also to the creation of a title in equity.²⁸ There was in that case “no identifiable property to which any trust could attach”.²⁹ Their Lordships’ advice does not contain any reference to certainty of subject matter as such.

Nonetheless, identifiability is discussed in connection with certainty in the texts. For example, under the heading of certainty of subject matter, McCormack states that “[t]he property which is said to form the subject-matter of the alleged trust must be identifiable”.³⁰ According to Moffat,

[a] purported trust will be void if the property intended to form the subject matter cannot be clearly identified. Expressions such as ‘the bulk of my residuary estate’... are too uncertain. ... It is only existing property - eg negotiable instruments, money,

²³ The Act does not define unascertained goods but logic suggests that they are goods which have not been agreed on and identified at the time that the agreement to sell is entered into. They are generic rather than specific.

²⁴ Section 18 and s 20 Rule 5 (1).

²⁵ [1986] PCC 121.

²⁶ At 137.

²⁷ [1994] 3 NZLR 385.

²⁸ At 393.

²⁹ At 397.

³⁰ McCormack, *G Proprietary Claims and Insolvency* (1997) 68.

chattels, interests in land whether in possession or remainder - that can form the subject matter of a trust.³¹

The latest edition of Pettit opens its discussion of certainty of subject matter by quoting Lord Browne-Wilkinson's third principle before going on to say,

but the requirement of certainty of subject is somewhat ambiguous for the phrase may mean that the property subject to the trust must be certain, or that the beneficial interests of the cestuis que trust must be certain.³²

As is apparent from the above, the absence of identifiable trust property is fatal to the creation of a trust. What is also apparent is that the learned authors are treating identifiability as if it were synonymous with certainty. As this article will suggest that Lord Browne-Wilkinson's identifiability principle goes beyond simply requiring "specified" "particular" or "defined" property (semantic certainty) to establish a trust and focuses on the need for defined property to be impressed with the trust, it is appropriate to examine here whether in fact certainty and identifiability are always employed to cover precisely the same ground. Clarke, discussing property, certainty and identifiability, does distinguish between the latter two concepts:

...[while]... certainty of subject matter is essential in the sense that you cannot have a property interest in a thing that does not exist ...[h]owever, does it necessarily follow that the thing must also be *identifiable* ? If the thing in question is in existence, and is in the hands of A, is it possible for B to claim a proprietary interest in the thing if it is impossible to distinguish it from other like things also in existence and also in the hands of A?³³

She goes on to discuss three cases in which in effect all the plaintiffs were claiming that they owned x out of the $x + y$ items held by the defendant, but could not say of any one item held by the defendant whether it was or was not their property. She poses the question: "Does this difficulty - essentially one of identification - rule out a proprietary claim?" In *Hunter v Moss*,³⁴ both certainty and identification are mentioned. Here the owner of 950 identical shares in Moss Electrical Co Ltd had orally declared a trust of 50 shares in favour of the plaintiff without indicating which of the 950 shares were to form the subject matter of the trust. The defendant argued that there

³¹ Moffat, *G Trusts Law Text & Materials* (2nd ed, 1994) 127 and 129.

³² Pettit, *P Equity and the Law of Trusts* (8th ed, 1997) 44. In this article the discussion of certainty is limited to the first of the two usages listed by Pettit.

³³ Clarke, "Property Law" (1995) 48 CLP 113-115.

³⁴ [1994] 3 All ER 216. (This case is discussed in the article by Clarke, *ibid*).

was no certainty as there was no identification of the 50 shares. The Court of Appeal referred to the need for certainty of subject matter and held that a declaration of trust in respect of a specific number of shares in a named company was sufficiently certain “without any further identification of their numbers”.³⁵ While this case has been criticised³⁶ in light of the subsequent judgment in *Re Goldcorp Exchange*,³⁷ the distinction that is made in it between certainty and identification has not been challenged.

Both the judgment in *Hunter v Moss* and Clarke’s article clearly treat certainty and identification as separate matters, which raises the question as to why the same distinction has not been made by text writers. It is suggested that this distinction has been overlooked because semantic uncertainty or the failure to define the subject matter of the trust with sufficient specificity, and the failure to identify which items out of a larger quantity of identical items are to be subjected to the trust both cause the alleged trust to fail for lack of subject matter (if *Hunter v Moss* is overruled by *Goldcorp*). However, whereas semantic uncertainty is fatal to the establishment of a trust, identification problems can be overcome. The problem is basically one of proper constitution or forging the link between the obligation and the property. As Oliver J put it in *Re London Wine*:

I cannot see how, for instance, a farmer who declares himself to be a trustee of two sheep (without identifying them) can be said to have created a *complete and perfect trust*...and it would seem to me to be immaterial that at the time he has a flock of sheep out of which he could satisfy that interest.³⁸ (emphasis added)

Identification problems seldom arise where the settlor creates an express trust by transferring property to trustees since “necessarily it must be clear what property has been transferred so as to be held on trust”.³⁹ Any problems as to whether the trust has been properly constituted usually arise from non-compliance with the formalities prescribed for transfer of certain types of property.

If, however, the trust is to be constituted by a declaration of trust, and the settlor intends to create a trust out of a larger bulk of assets owned by him as

³⁵ At 220.

³⁶ Hayton, “Uncertainty of Subject Matter of Trusts” (1994) 110 LQR 335, and Ockelton, “Share and Share Alike?” (1994) CLJ 448.

³⁷ [1994] 3 NZLR 385.

³⁸ [1986] PCC 121, 137.

³⁹ Hayton D, *The Law of Trusts* (2nd ed, 1993) 75-76. There may still be problems in the exceptional cases referred to therein.

in Oliver J's example above,⁴⁰ identification problems can arise as to which of his property the settlor intended the trustee obligation to relate.⁴¹ In such cases the declaration of trust does not of itself transfer the equitable title; the identification process is also necessary. Initial identification problems can be cured if the property is subsequently identified so as to create "a complete and perfect trust".

The mechanics of "identifying" property so as to constitute the trust and transfer the equitable title will be discussed in part V below.

2. *Identifiability in the context of tracing*

Tracing in the trust context is a process used to identify the plaintiff beneficiary's original property or its exchange product in the hands of the defendant or third party, to enable the plaintiff to bring a proprietary claim against a particular item of property or fund. It is the process of following property through changes in form that enables a beneficiary to identify misapplied trust property through one or more substitutions.⁴²

A proprietary claim is particularly desirable if the misapplying trustee has since become insolvent, thus rendering a personal claim futile. Tracing would be appropriate if, for example, a trustee who has since become bankrupt had misappropriated trust funds to buy a valuable painting for her husband. If he still has the painting the beneficiary can trace the trust funds into this substitute asset in his hands and make a proprietary claim in respect of it. The link between the funds and the painting is fairly direct, but what if, instead of buying her husband a painting with the misappropriated funds, the trustee had simply deposited the funds in her husband's bank account? No proprietary claim can succeed unless a plaintiff can identify his property in the defendant's hands,⁴³ so the question arises as to how one identifies funds in an account which may, at the time the trust funds are deposited, be either in credit (that is, where the bank owes money to the account holder) or in debit (that is, where the account holder owes money to the bank). The answer lies in equity's rules and presumptions which enable the trust beneficiaries to identify their property in the hands of the trustee or an

⁴⁰ No problem arises if the trust is declared in such a way as to make any further identification unnecessary, eg "all my sheep" or "all the sheep on my Te Kuiti farm", or "my sheep earmarked with the numbers 15 to 45 inclusive".

⁴¹ Hayton, D (ed) *Underhill and Hayton Law of Trusts and Trustees* (15th ed, 1995) 125.

⁴² McCormack, G *Proprietary Claims and Insolvency* (1993) 170-171.

⁴³ Jones, G (ed) *The Law of Restitution* (4th ed, 1993) 75.

innocent volunteer.⁴⁴ These tracing rules are set out at length in all standard trusts texts. However, one such rule, particularly relevant to a discussion of *Westdeutsche*, is that, if the plaintiff's property or its exchange product disappears, as for example money would if deposited in a bank account which was or subsequently became overdrawn, the right to trace is lost.⁴⁵

3 Comparing the different uses of the concept of identifiability in trust law

As has been seen, the concept of identifiability performs two distinct functions in trust law. First, identifiability determines whether there is the requisite property for a trust to be established and as such is relevant to the proper constitution of the trust. Secondly, in misapplication cases, equity's identification principles determine whether there are any surviving trust assets (either in their original form or in exchange products) which can be traced and made the subject matter of a proprietary claim.

Whereas lack of identifiability in the first sense means that no trust comes into existence, lack of identifiability in the second sense has no bearing on the existence of the trust but limits the remedy available for breach of a properly constituted trust to the personal claim.

In practical terms this means that a claimant who wishes to assert a proprietary claim in respect of particular assets, on the basis that they are held for her on trust, might first use the concept of identifiability to establish that that property was impressed with a trust. Secondly, and quite independently of the previous use, if that property had either changed hands or changed form, or both, she would use the concept to establish whether any identifiable property remained. If there is no identifiable property in the first sense then there is no need to discuss identifiability in the second sense. This seems obvious, but it is submitted that in both *Westdeutsche* and in *Gallen J's* judgment in *Fortex* the two steps seem to flow into each other.

III. THE BACKGROUND FACTS AND APPLICATION OF THE IDENTIFIABILITY PRINCIPLE IN *WESTDEUTSCHE*

Westdeutsche Landesbank Girozentrale (the Bank) had entered into an interest rate swap agreement with Islington Borough Council (the Council) involving an up front payment to the Council on 18 June 1987 of 2.5 million pounds. The money was credited to a bank account containing other Council money which became overdrawn later that month. Such transactions were

⁴⁴ *Ibid*, 92.

⁴⁵ *Ibid*, 91.

subsequently found to be ultra vires local authorities. The Bank sought restitution of the balance of the up-front payment, minus payments made, plus compound interest. The sole issue in the House of Lords was the availability of compound interest. The majority of their Lordships refused to depart from the traditional position that compound interest was only available in equity. They examined whether a claim in equity was available on the basis that the payments made under the ultra vires contracts gave rise to a resulting trust and concluded that it was not.

As mentioned in the introduction, Lord Browne-Wilkinson prefaced his judgment with a general discussion of trust principles. The purpose of this part of the article is to analyse the application of the third principle within its context to establish what His Lordship meant when he referred to “identifiable trust property”. It will be suggested that this aspect of the judgment is far from clear. First, there is a hint of tautology about the statement that “[i]n order to establish a trust there must be identifiable trust property”. Could his Lordship have simply said “In order to establish a trust there must be identifiable property” or does the repetition of “trust” add something? Secondly, it is not totally clear which of the two senses of “identifiable” discussed above that His Lordship has in mind in some passages of the judgment. Thirdly, the judgment also refers to “defined trust property”. Is this phrase a synonym for “identifiable trust property”?⁴⁶

Lord Browne-Wilkinson’s first reference to identifiability in the context of the facts of the case came when, having established his fundamental principles, he said:

Those basic principles are inconsistent with the case being advanced by the bank. The latest time at which there was any possibility of *identifying* the ‘trust property’ was the date on which the moneys in the mixed bank account of the local authority ceased to be *traceable* when the local authority’s account went into overdraft in June 1987. At that date, the local authority had no knowledge of the invalidity of the contract but regarded the money as its own to spend as it thought fit. There was therefore never a time at which both (a) there was *defined* trust property and (b) the conscience of the local authority in relation to such *defined* trust property was affected. The basic requirements of a trust were never satisfied.⁴⁷ (emphasis added)

At first sight the juxtaposition of “identifying” with “traceable” in the second and third sentences of the above passage suggests that His Lordship is equating identifiable trust property with traceable property and using

⁴⁶ See Friar, “Equity, Restitution and Commercial Commonsense” [1996] NZLJ 448.

⁴⁷ [1996] 2 All ER 961, 988-989.

identifiability in the second of the two senses discussed above. However, the repeated reference to “time” in the second and penultimate sentences of that paragraph suggests that His Lordship regards “trust property” as “identifiable” when two factors coincide: (a) there is defined trust property; and (b) the conscience of the alleged trustee in relation to the defined trust property is affected.

There is an immediately apparent difficulty with this passage in that both (a) and (b) refer to defined “trust” property. With reference to that expression in (a), if there is defined *trust* property then in the very nature of things the conscience of the owner of the legal title is affected, otherwise it would only be defined property. Similarly, in (b), if the conscience of the legal title owner is affected in relation to trust property it must be defined. If however the reference to “trust” is omitted from (a) and (b),⁴⁸ this difficulty disappears. It can then be suggested that what Lord Browne-Wilkinson meant in his third principle is that there is identifiable trust property so that a trust is established or constituted when the link between defined property and the conscience of the alleged trustee is present. This link could be, and in the case of an express trust would be, expressed in terms of property being “impressed” with the trust or the trust being constituted. In other words, what looks like a single requirement “identifiable trust property” seems to be comprised of two elements: (a) defined property; and (b) some knowledge or conduct in relation to the defined property which has the effect of “impressing” it with the trust so that the trust is properly constituted.

Accordingly, the identifiability principle could be expressed that, to establish a trust, defined property must be impressed with the trust. This formulation makes it explicit that the principle contains the requirement for both semantic certainty of subject matter *and* proper constitution of the trust. It also explains why, instead of simply stating, “[i]n order to establish a trust there must be identifiable property”, His Lordship required “identifiable

⁴⁸ Support for editing His Lordship’s words in this fashion can be found in the passage under scrutiny. In the second sentence of that paragraph he has put speech marks around the words “trust property” which suggests that whether the property was or was not trust property was being left undecided for the time being. Used in this way “trust property” seems to be shorthand for “the property which is said to form the subject-matter of the alleged trust”. In parts (a) and (b) of the penultimate sentence of the paragraph the speech marks do not re-appear and this may well be an accidental omission. As suggested, the problem in (a) and (b) can be avoided by omitting the word trust altogether or alternatively, and in keeping with the beginning of the paragraph, by placing that word in speech marks.

trust property”, as this phrase underlines the requirement that the property has to be identifiable *as trust property*. The only property identifiable as trust property is property which has been impressed with the trust. He is not using “identifiable” simply as a synonym for “defined”. To be identifiable, property must be defined but that alone is not sufficient. As used by Lord Browne-Wilkinson in his third principle, “identifiable” comprehends “defined” but has a wider meaning as explained above.

Applying this to the facts of *Westdeutsche*, defined property (in the form of a specific sum of money from the bank which was deposited into the local authority’s account) had existed but no trust was ever established in respect of it. No trust could be established because, before the defined property could be impressed with any trust obligation (that is, before the local authority realised the loan was illegal), it had ceased to exist. This happened because the bank account into which the local authority had originally deposited the loan money went into overdraft shortly after the money was deposited and before the local authority knew anything which could affect its conscience (that is, before it could become a trustee). No opportunity for the local authority to act unconscionably in relation to the money arose. The money had gone before the local authority had sufficient knowledge to attract the label of unconscionable conduct to anything that it may have done with the money had it still been available. The defined property was never impressed with a trust. It was never transformed into “identifiable trust property”. No trust was ever constituted in respect of it.

Against the above interpretation of the third principle it might be argued that Lord Browne-Wilkinson was using “identifiable” to mean “defined” and nothing more. This interpretation overlooks the fact that “*identifiable*” and “*defined*” are not exact matches as are “*identifiable*” and “*definable*” or “*identified*” and “*defined*”. Nor are the words exact synonyms. Property is “defined” when its nature, properties or essential qualities are described or fixed with precision or when its boundary or extent is determined.⁴⁹ Property is “identifiable” when it can be proved or recognised as being a certain thing or when its identity can be established.⁵⁰

Property that is not defined with sufficient certainty can never become trust property. A trust cannot be established in respect of “most of my blue chip shares” because the phrase “blue chip shares” has no precise meaning, and even if it had the extent of the trust property is rendered vague by the phrase “most of”. On the other hand, defined property which is not currently

⁴⁹ Hanks, P (ed) *Collins English Dictionary* (1979) 389.

⁵⁰ *Ibid*, 728.

identifiable trust property can become so. For example, if I have 20 cases of 1995 Cloudy Bay Sauvignon Blanc in my wine cellar and declare on the birth of my first child that I will hold 10 cases on trust for her until she is 21, those 10 cases will only become identifiable trust property when I take the appropriate steps to impress them with the trust. Precisely what those steps are will be discussed in greater detail in part IV below.

His Lordship's first reference to "defined trust property" has already been discussed above in the context of the argument that identifiable has a wider meaning than defined. Later in the judgment he refers to "defined trust property" in the context of a restitutionary argument to extend the definition of the resulting trust:

The search for a perceived need to strengthen the remedies of a plaintiff claiming in restitution involves, to my mind, a distortion of *trust principles*. First, the argument elides rights in property (which is the only proper subject matter of a trust) into rights in 'the value transferred'. A trust can only arise where there is *defined trust property*: it is therefore not consistent with *trust principles* to say that a person is a trustee of property which cannot be defined.⁵¹ (emphasis added)

There are two references to trust principles in this paragraph. Does this mean that, if one read backwards from this passage to His Lordship's original statement of "[t]he relevant principles of trust law", principle (iii) could now equally well read "[i]n order to establish a trust there must be *defined* trust property" or as His Lordship puts it "[a] trust can only arise where there is defined trust property".⁵²

It is suggested that it should not be so interpreted. His Lordship's sole object in the passage above is to dispel any notion that there can be a trust in the absence of property. He is not concerned here with the requirements for establishing or constituting a trust as he was when he stated his third principle. He is focussing instead on the permissible subject matter of a trust. His sole concern is to limit trusts to "defined trust property" so as to exclude the possibility of a trust arising in respect of "the value transferred". He is stressing the role of property within the trust concept and making the same point as the authors cited in Part I made, namely, that defined, specified or particular property is essential.

⁵¹ [1996] 2 All ER 961, 991.

⁵² This is the sense in which Friar understood it when he paraphrased the third principle as "there must be defined trust property" (Friar, *supra* note 46).

The possibility that Lord Browne-Wilkinson was using identifiable in the tracing sense in the passage quoted above⁵³ has already been discussed and dismissed. However, when he next speaks of an identifiable trust fund in a later and separate section of the judgment, he again seems to be doing so in the tracing context:

[Counsel for the Bank's specific disavowal of a constructive trust] was plainly right because the local authority had no relevant knowledge sufficient to raise a constructive trust at any time before the moneys, upon the bank account going into overdraft, became *untraceable*. Once there ceased to be an *identifiable* trust fund, the local authority could not become a trustee: *Re Goldcorp Exchange Ltd (in receivership)* [1994] 2 All ER 806...⁵⁴ (emphasis added)

This is a puzzling passage. The last sentence would make more sense if the reference to an identifiable trust fund was replaced with the words identifiable fund. The reference to there ceasing to be an identifiable *trust* fund suggests that there had been a trust fund at some stage which, as a result of the tracing rules relating to trust funds deposited into accounts which are or subsequently become overdrawn, had ceased to exist. This must be incorrect. As discussed above there had been a defined fund in the form of the loan moneys. That fund had ceased to exist (upon the account going into overdraft) before it could be impressed with any trust. The facts which potentially could have given rise to a constructive trust in respect of that defined fund were not known until after it had been dissipated. There was no subject matter onto which any trust obligation could fasten. As no identifiable trust fund ever existed His Lordship's reference to an identifiable trust that had ceased to exist is inexplicable.

In summary, the meaning of identifiable trust property used by His Lordship in formulating and applying his trust principles is not clear. Three interpretations are possible:

1. Identifiable is synonymous with traceable. There are passages in the judgment where the word seems to be used in this sense. However, this cannot be the case where it appears in the third principle which relates to the establishment of a trust. Tracing has nothing to do with the establishment of a trust and can only take place in relation to property in respect of which a trust has previously been established.

⁵³ Supra note 51.

⁵⁴ At 990.

2. Identifiable means no more than defined in the sense that trust property must be defined or described in terms which have precise and certain meaning. It requires no more than semantic certainty. Against this it has been argued that identifiable and defined are not synonyms.

3. Identifiable means that, not only must trust property be defined, it must also be impressed with the trust so that it is identifiable as trust property.

It is submitted that the third interpretation is correct. Not only does it explain the otherwise tautologous repetition of trust in the phrase “identifiable *trust* property”, but it is also consistent with the recent comments of the Court of Appeal in *Fortex*.⁵⁵

IV. THE MECHANICS OF IDENTIFYING PROPERTY AND CONSTITUTING THE TRUST

As has already been discussed in section 3 of Part II above, identification difficulties arise most frequently in trust law where the settlor has attempted to constitute the trust by making a declaration of trust in respect of a specified number of items in circumstances where she owns a larger number of identical items. Similar attempts to establish an equitable title to property by invoking the trust concept in sales of unascertained goods have failed for the very same reason that it is impossible to establish legal title under the Sale of Goods Act 1908 (“it is impossible to have a title to goods when nobody knows to which goods the title relates”).⁵⁶ In these circumstances, “precise identification is just as much a requirement of equity as of law”.⁵⁷

The analogy between the transfer of property in sale of goods cases and the constitution of trusts has been drawn by Sealey and Hooley:

Just as property cannot be transferred in unascertained goods, so also we may note that there cannot be a valid trust of unidentified property.⁵⁸

Accordingly, the mechanics by which property passes under the Sale of Goods Act in relation to an agreement to sell unascertained goods provide a guide as to how unascertained goods can become identifiable trust property.

⁵⁵ *Fortex Group Ltd (in receivership and liquidation) v MacIntosh* [1998] 3 NZLR 171, 175, where Tipping J spoke of the need for “a separately identifiable fund”.

⁵⁶ *Re Goldcorp Exchange Ltd* [1994] 3 NZLR 385, 395.

⁵⁷ Goode, “Ownership and Obligation in Transactions” 103 LQR 433, 449.

⁵⁸ Sealey, L and Hooley, R *Text and Materials in Commercial Law* (1994) 264.

The Sale of Goods Act 1908 contemplates two types of goods, specific and unascertained. Property in specific goods passes when intended to,⁵⁹ but no property passes in unascertained goods until they are ascertained by appropriation to the contract.⁶⁰ Where the contract is for specific goods, there is no identification problem as by definition specific goods are “goods identified and agreed on at the time a contract of sale is made”.⁶¹

Unascertained goods are not defined by the Act but logic suggests that they are goods which have not been identified and agreed on at the time of the contract so that the contract is in respect of generic rather than specific items. Nor does the Act distinguish between goods that are *wholly* unascertained, in that the parties have not even designated a source of supply in their contract, and those goods that are *partially* identified as a result of agreement between seller and buyer that they shall be supplied from an identifiable bulk.⁶²

Professor Goode calls partially identified goods “quasi-specific” goods and confines his use of unascertained goods to goods which are wholly unascertained and notes:

Goods can move (figuratively) from an unascertained to an ascertained state directly by an act of appropriation sufficient for precise identification. Alternatively there can be a staged progression, from unascertained to quasi specific (as the result of a post-contract agreement that the goods shall be supplied from an identifiable source or bulk) and thence to ascertained goods through appropriation from that bulk.⁶³

He is suggesting that where unascertained goods rather than specific goods are involved precise identification requires appropriation:

Where the contract is for the sale of unascertained or quasi-specific goods, two stages of identification separated by an interval of time are involved. At the moment the contract is made, the parties must, as terms of the contract, agree upon the characteristics by which the goods to be supplied are to be identified. This means at least some verbal description, whether in writing or by word of mouth, but in many cases the difficulty of expressing in words all the relevant characteristics of the required article makes it desirable for the description to be supplemented by other

⁵⁹ Section 19.

⁶⁰ Section 18 and s 20 Rule 5(1).

⁶¹ Section 2.

⁶² The same distinction was drawn by Lord Mustill in *Re Goldcorp Exchange Ltd* [1994] 3 NZLR 385, 392-393 between “generic goods “ and “goods sold ex-bulk”.

⁶³ Goode, *R Commercial Law* (1982) 218.

methods, eg a sample, photographs, drawings...(etc). At the second stage, goods possessing the specific characteristics must be set aside and appropriated to the contract, so that the seller ceases to be entitled to proffer or the buyer to take other goods, even if having all the designated characteristics.⁶⁴

The importance of appropriation is stressed by Oliver J in *Re London Wine Company (Shippers) Ltd*:

Section 16 [section 18 of the New Zealand statute] states quite clearly that the property is not transferred to the buyer unless and until the goods are ascertained but it is not a necessary corollary of this that the property *does* pass to the buyer when they *are* ascertained. To produce that result one either has had to find an appropriation (from which an intention to pass the property will be inferred) or one has to find an intention manifested in some other way.⁶⁵

In that case the company was an insolvent wine dealer which had stocks of wine in several warehouses. Some of the wine had been sold to customers for laying down or investment purposes. Although it was clearly contemplated that the wine would belong to the purchasers and would be stored by the company, no appropriation from the bulk of the wine in storage had been made to answer any particular contracts. In the absence of appropriation by earmarking or otherwise setting aside each purchaser's wine, legal property did not pass under the Sale of Goods Act, nor had the company created a completely constituted trust sufficient to pass the equitable title.

The Privy Council expressed its entire agreement with this case in *Re Goldcorp Exchange Ltd*.⁶⁶ Accordingly, where the alleged sale or trust involves goods forming an unidentified part of a bulk of identical goods, specific appropriation is required to transfer legal and equitable title alike.

According to Professor Hayton, in an article strongly critical of *Hunter v Moss*, the position is the same irrespective of whether tangible or intangible assets are involved. He stated that "[i]ndeed 'Equity follows the law', so surely one needs a specific appropriation where concerned with assets forming an unidentified part of a fungible bulk".⁶⁷

He makes the same point as editor of *Underhill and Hayton* :

⁶⁴ Ibid, 220.

⁶⁵ [1986] PCC 121, 150.

⁶⁶ [1994] 3 NZLR 385, 401.

⁶⁷ Hayton, "Uncertainty of Subject Matter of Trusts" 110 LQR 335, 336.

No problems arise as to certainty of subject matter of a declaration of trust where the settlor's declaration relates to specific property, eg 'my one and only Picasso painting, all my shares in ICI plc, all my money currently in my Woolwich building society account'. However, if it relates to part of his unascertained property in which he retains an interest, no trust can arise till there has been a segregation or appropriation of specific property out of the larger mass of property, eg where it is intended to create a trust of 20 out of 80 cases of Chateau Latour 1982 in the settlor's cellar or of 1000 pounds out of 5000 pounds in the settlor's Woolwich Building Society account.⁶⁸

Professor Martin has suggested that *Hunter v Moss* could be distinguished from another case⁶⁹ involving intangible assets in which the alleged trust failed because no identifiable assets had been impressed with the trust. The basis of the distinction is that, in the former case, the bulk from which the trust was carved was identified (that is, the 950 shares in MEL), whereas in the latter case it was not. If this was the case a declaration of trust in respect of \$x out of a designated bank account with a larger balance would be valid.⁷⁰

This cannot be correct. Although we might refer colloquially to our "money in the bank", no money matching the balance of our account is physically held for us. Instead, money paid into a bank account ceases to be the depositor's money and becomes the bank's on the basis that it will repay the money when called upon to do so;⁷¹ the relationship between the bank and its customer is one of debtor and creditor (and *vice versa* if the account goes into overdraft). The customer, while her account is in credit, now owns a single indivisible asset in the form of a debt (as opposed to a number of units capable of segregation from a bulk) and cannot make a declaration of trust in respect of part of it.

As Professor Goode explains, "[a] participation in a debt is necessarily an interest in the entirety of the debt, not an interest in an undivided part of the debt...".⁷² Accordingly, Professor Hayton's approach is to be preferred. To constitute properly a trust in respect of "1000 pounds out of 5000 pounds in the settlor's Woolwich Building Society account", the settlor would have to

⁶⁸ Hayton, D (ed) *Law of Trusts and Trustees* (15th ed, 1995).

⁶⁹ *MacJordan Construction Ltd v Brookmount Erostin Ltd* [1992] BCLC 350. The explicit approval of this case in *Re Goldcorp Exchange* [1994] 3 NZLR 385, 401 strongly suggests that *Hunter v Moss* was wrongly decided.

⁷⁰ Martin, J (ed) *Modern Equity* (15th ed, 1997) 97.

⁷¹ *Foley v Hill* (1848) 2 HL Cas 28,36.

⁷² Goode, *supra* n 57, at 448.

segregate or appropriate the 1000 pounds by withdrawing it from that account. Only then could it become identifiable trust property within the meaning of Lord Browne-Wilkinson's third principle.

This is consistent with the joint judgment in *Fortex*, which regarded a "separately identifiable fund" as essential to the imposition of an institutional constructive trust.

VI. CONCLUSIONS

My submission is that Lord Browne-Wilkinson's identifiability principle requires defined property to be impressed with the trust so that equitable title to the property passes to the beneficiary and the trust is properly constituted. I submit also that the principle is not satisfied if the property alleged to form the subject matter of the trust is not defined with semantic certainty. Nor is it satisfied if the property alleged to form the subject matter of the trust, although semantically certain, has not been subjected to any trust obligation so as to transfer equitable title and constitute the trust.

The issue of identifiability sufficient to establish a trust has arisen several times in recent years (frequently within a sale of goods context) and has not been consistently dealt with. Lord Browne-Wilkinson's identifiability principle, stated in wide terms and embracing all types of property and express, implied and institutional constructive trusts alike, as interpreted above, clarifies this issue. The tenor of the joint judgment in *Fortex* on this point indicates that the Court of Appeal is thinking along similar lines in so far as the institutional constructive trust is concerned.

THE CIRCUMSTANCES AS SHE BELIEVED THEM TO BE: A REAPPRAISAL OF SECTION 48 OF THE CRIMES ACT 1961

BY FRAN WRIGHT*

I. INTRODUCTION

According to section 48 of the Crimes Act 1961, “[e]veryone is justified in using, in the defence of himself or another, such force as, in the circumstances as he believes them to be, it is reasonable to use”. This provision is subjective, in that the “circumstances” are viewed through the defender’s eyes. The question is what the defender believed was happening rather than what was “really” happening. If she believed that she was about to be killed, her self-defence claim is assessed as if she really was about to be killed. However, when her response to this threat is considered, there is an objective test. It is not enough for the defender to say that she *believed* her reaction was reasonable: she must have used an amount of force that would have been reasonable had the circumstances been as she believed them to be.

The subjective test is important in cases of mistake, where there is a difference between the circumstances as the defender saw them and as they “really” were. However, courts have sometimes failed to take a relevant mistake into account. They have applied section 48 correctly in cases of mistake about whether a threat exists or about how serious a threat is. They have not usually looked at the defender’s own beliefs about whether it is possible to escape from an aggressor or about whether non-violent options are available. Assessing a defender’s use of force as if she was able to make use of all the options that were actually available, without allowing for any mistakes that she might have made about those options, is contrary to the words and the spirit of section 48. Any belief about a fact upon which the objective reasonableness of a defender’s response depends, is a belief about the circumstances for the purposes of section 48, and the defender should be treated as if that belief was correct.

The approach taken in this article is to treat the issue as one of statutory interpretation: what do the words of section 48 mean? The validity of the honest belief test will not be questioned. To do so would distract from the very real problems of interpretation posed by section 48. Because of the way in which the issue has been defined, there will be little reference to the theoretical literature on self-defence. The dominant approach to self-defence

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among philosophers and criminal law theorists rejects the honest belief test in force in New Zealand: indeed, they express doubts about the validity of the reasonable belief standard that applies in most common law jurisdictions.¹ For this reason the preoccupations of the theoreticians are not the same as those of the criminal lawyers, and their writing does not deal with the questions posed in this article. The majority of material referred to will therefore come from “mainstream” criminal law.

II. THE COURTS' INTERPRETATION OF SECTION 48 OF THE CRIMES ACT 1961

Self-defence justifies a person's use of force. This means that the person who meets the requirements of section 48 has acted lawfully. For this reason, the burden of disproving self-defence lies upon the Crown.² This does not mean that self-defence must be negated every time a person is charged with a crime of violence; the rule is that self-defence should be put to the jury only where the evidence as a whole establishes a “credible narrative”, one that leaves open a reasonable possibility of self-defence.³

According to Hammond J,

Self-defence involves three elements. The first is whether the force used by the accused was in defence of himself. The second is an inquiry as to the circumstances as the accused believed them to be. The third inquiry is as to whether the force used was reasonable in the circumstances as the accused believed them to be.⁴

These elements will now be considered in more detail.

Self-defence is available only to those whose intention in using force is to defend themselves. If the reason for causing that harm is something other than defence, the fact that the victim was an aggressor does not make the defendant's actions lawful.⁵ However, an intention to kill or cause some lesser degree of bodily harm is not inconsistent with self-defence.⁶

¹ See eg Uniacke, S *Permissible Killing: The Self-Defence Justification of Homicide* (1994) chapter 2, and Schopp, “Self-Defence” in Coleman, J and Buchanan, A (eds) *In Harm's Way* (1994).

² *R v Robinson* (1987) 2 CRNZ 632, 635 (CA).

³ *R v Tavete* (1987) 2 CRNZ 579, 581 (CA).

⁴ *R v McKay* [1997] 3 NZLR 199, 200 (HC).

⁵ *R v Dadson* (1850) 3 Car & Kir 148, 4 Cox CC 358.

⁶ Prior to 1980, this was clear from the statutory definition of self-defence. The current provision says nothing about intent but there is no reason to suppose that a new

The second inquiry is the subjective phase of the defence. This phase is unnecessary if “the circumstances” and “the circumstances as she believed them to be” are the same. However, where a mistake has been made, the defender will be treated as if this aspect of the circumstances was as she believed. It does not matter that her mistake is unreasonable or that it is the result of intoxication.⁷ The subjective test is illustrated by *McKay v Police*.⁸ McKay was attacked by Scott and responded by punching him. This broke Scott's jaw, and Scott fell to the ground. He was clutching McKay's leg, trying to pull himself up, but McKay did not realise that Scott was injured and thought that the attack was continuing. He therefore hit him again. McKay was initially convicted of assault because the second series of blows were unnecessary “in that [he] knew that Mr Scott was suffering the effects of alcohol and that he had been put down by a blow to the jaw”.⁹ McKay's appeal succeeded. If the circumstances had been as he believed them to be, the fight had not come to an end and it was not unreasonable to continue defending himself.¹⁰

Whether the force used by a self-defender is reasonable depends on whether it was reasonably necessary to use force and on whether the harm caused was reasonably proportionate to the harm sought to be prevented.

Whether force is necessary is answered by asking whether the steps taken were the minimum that would be needed to stop the attacker. The ability to retreat is relevant to whether the response was necessary but there is no legal

restriction was being imposed. Such a restriction would be inconsistent with common law: the Privy Council in *Palmer* stated that if a person uses deadly force in defence and his or her actions were within the scope of the legal defence, “he is not guilty of any crime even if the killing was intentional” (*Palmer v The Queen* [1971] AC 814, 823). Case-law applying s 48 seems consistent with this. In *R v Ranger* (1988) 4 CRNZ 6 (CA), for instance, the Court ordered a retrial because the jury was not directed on self-defence. It was clear that the appellant had intended either to kill or to cause grievous bodily harm to her partner - he was stabbed in the shoulder - but there was no suggestion that this intent was inconsistent with self-defence. (This example is taken from Simester, A and Brookbanks, *W Principles of Criminal Law* (1998) 413-414).

⁷ The evidence for this assertion is that in many cases involving mistakes about defence it is clear from the facts that the defender was intoxicated, but the courts do not discount the mistake. See eg *Stanbury v Police* (1988) 3 CRNZ 253.

⁸ *Supra* note 4.

⁹ At 200.

¹⁰ At 210.

duty to retreat.¹¹ It can be reasonable to use force before a threatened attack is launched. A person who is facing a knife is not expected to wait until the knife has been used on her: it may be necessary to pre-empt the attack.¹²

Proportionality refers to the relationship between what is stopped or averted and the force used to stop or avert it.¹³ Killing is likely to be disproportionate unless the threat is itself of death or very serious injury. The courts do not apply a strict proportionality test, however:

...a person defending himself cannot weigh to a nicety the exact measure of his necessary defensive action.¹⁴

In considering whether a defender's use of force was reasonable, therefore, it is necessary to look at what was threatened and what the defender could do about it. Submission, flight, or calling for help might be more appropriate than using force. The problem is that a defender's beliefs about whether flight or assistance would be possible or effective might be mistaken. It is not clear whether section 48 requires the court to treat the defender as if these beliefs were correct. Most mistake cases are concerned with mistakes about whether a threat exists and the courts have not dealt with mistakes about alternatives to using force in a consistent manner. This is the difficulty with the section with which this article is concerned.

Subjective beliefs about the availability of assistance were taken into account in *Crowe v Police*.¹⁵ Crowe and some friends were set upon by an older group. Crowe managed to push off his assailant and went to assist his friend, Mokomoko, using the metal liner of a rubbish bin as a weapon. The trial judge found that Crowe's actions were unreasonable: the police were nearby and Crowe should have gone to them for protection for himself and his friend rather than using force.¹⁶ Crowe's appeal succeeded. Williamson J emphasised Crowe's view of the circumstances. He had said that when a police car drove by, "he and his friends whistled out and shouted to try and get them to stop, but that it went on and he did not know whether the Police

¹¹ *R v Terewi* (1985) 1 CRNZ 623, 625.

¹² At 625; also *R v Wang* [1989] 3 NZLR 529, 539.

¹³ What matters here is the amount of force that the defender intends to use, so that, if a defender strikes an aggressor intending to cause minor injury and in fact causes a more serious injury, the question will be whether that minor injury was disproportionate.

¹⁴ *Palmer*, supra note 6.

¹⁵ Unreported, High Court Christchurch, AP 65/88, 10 June 1988, Williamson J.

¹⁶ At 5. The cause of Crowe's "impairment" was, presumably, the glue he had sniffed.

had heard them or not”.¹⁷ If the police had just refused to stop and assist, it was not unreasonable to resort to self-help, so Crowe's response was a reasonable one.

However, beliefs about whether assistance is available have not been treated in this way in other cases. Mistakes that a reasonable person would make in the same situation are taken into account when the objective reasonableness of force used is assessed, but other mistakes are ignored. This can be seen by comparing two cases, *Jenkins*¹⁸ and *Wang*.¹⁹

Jenkins and his friends were ejected from a nightclub after a dispute with another group. They were followed onto some steps. Jenkins was punched but managed to escape; his friend Marie was less lucky, becoming trapped further up the steps. Marie was screaming and yelling; Jenkins threw a milk bottle in the direction of the assailants and they retreated a little. The police then arrived and arrested Jenkins. His answer to a charge of disorderly behaviour was that he threw the bottle in defence of Marie, but the District Court Judge thought that this was unreasonable and convicted him. On appeal, McGechan J disagreed:

I can infer readily enough that by the time a telephone had been found at that hour on a Saturday night or a patrol car located and the police arrived the feared injury may well have occurred and that would have been evident to [Jenkins]. That was not a realistic option.²⁰

The trial judge's failure to take the difficulty of finding a police officer into account was an error; the High Court regarded this as an important part of “the circumstances”. This case seems to be an example of a mistaken belief about the availability of assistance being taken into account, but the way in which it was done was not the same as in *Crowe*.

McGechan J started with how he saw the situation himself and finished with the assumption that that must have been how Jenkins himself saw it. The implicit question was not “what did Jenkins believe about the availability of police assistance” but “what would a reasonable person have believed about the availability of police assistance”. This is not, therefore, a fully subjective approach: if it was, Jenkins' views would have taken centre stage and what the judge thought would have been irrelevant.

¹⁷ At 3.

¹⁸ *Jenkins v Police* (1986) 2 CRNZ 196.

¹⁹ *Supra* note 12.

²⁰ (1986) 2 CRNZ 196, 199.

This did not make any difference to the outcome because the judge clearly thought Jenkins' mistake was reasonable: it was a belief the judge himself would have held in the same circumstances and McGechan J defined "the circumstances" for the purposes of section 48 to include the apparent non-availability of police assistance. This approach does not always produce the same result as a wholly subjective approach, however: a problem arises if the defender's beliefs are not reasonable.

Wang was convicted of the murder of her husband Li. On the night of the homicide they had a party. Li became very drunk and forced Wang to telephone Hong Kong and demand money from family members. He made other threats as well, but eventually went to bed, where he passed out. Wang tied him up, tried to strangle him, stabbed him several times, and then smothered him with a pillow.

The trial judge did not allow self-defence to go to the jury because Wang's story did not satisfy the evidential burden.²¹ No reasonable jury could have decided that Wang had used reasonable force in self-defence.

Li was in a drunken stupor. It was found that:

One could not reasonably have considered that those threats might be carried out by him, 'at any moment', in his then state, nor when his aim was to extort money from her sister in Hong Kong. There was no immediate danger to render causing his death a reasonable course of action.²²

This meant that Wang's actions were unnecessary: there were other things she could have done to protect herself:

Her sister and her friend Susan were both in the house. She could have woken them and sought their help and advice. She could have left the house taking her sister with her in the car which was available. She could have gone to acquaintances in Christchurch or to the police....We are satisfied that no ordinary reasonable person...would...have believed it necessary to kill him.²³

Wang herself may have seen the circumstances differently. She had been physically, sexually and emotionally abused throughout the marriage. She was an immigrant to New Zealand and spoke little English. The Court of

²¹ There must be a "credible narrative which might lead the jury to entertain the reasonable possibility of self-defence" (*Tavete*, supra note 3, at 581).

²² [1989] 3 NZLR 529, 537.

²³ At 534.

Appeal admitted that she “was not conversant with social opportunities or avenues for help” and described this as a case of “a weakening of the accused’s ability to reason leading to a situation where in her own perception she was in a desperate situation with an apparent absence of alternatives”.²⁴

In *Jenkins*, although the subjective test was not applied to beliefs about alternatives to using force, the court was willing to consider the reasonableness of the appellant’s force as if there were no police officers within easy reach. This technique could not be used in *Wang*. Although *Wang* may well have believed that escape was not possible, this belief was ignored in the court’s reasoning about the reasonableness of her actions.

The Court of Appeal’s approach in *Wang* is consistent with *Jenkins* once it is recognised that it was the reasonableness of *Jenkins*’ beliefs that allowed them to be considered. The likely absence of police officers was part of the objectively-defined circumstances rather than part of the circumstances as the appellant believed them to be. Because *Wang*’s assessment of alternatives differed from that of a “reasonable” person - it was influenced by physical illness, depression and social isolation - it could not be seen as part of the objectively-defined circumstances.

Wang raises the question: what is the correct interpretation of section 48? *Crowe* was an example of a broad approach to “the circumstances” in which a belief about whether assistance is available or would be effective is a belief about the circumstances and therefore to be treated as if correct. *Jenkins* and *Wang* are examples of a narrower approach, in which the availability of assistance is an objective matter so that differences between the defender’s opinions about sources of assistance and those of the court are ignored. This effectively imposes a reasonableness test for some of a defender’s beliefs. The rest of this article will consider which interpretation is more consistent with the principles that underlie section 48 and with the intent of Parliament in enacting it in its current form.

III. THE ENACTMENT OF SECTION 48

Prior to 1980 different rules applied to those who defended themselves against provoked and unprovoked assaults. The law relating to defence against a provoked assault was much stricter, so that the availability of the defence could depend on who had started an incident. This led to difficulties in application of the law, which were exacerbated by uncertainty about the effect of mistakes. Some of the relevant sections of the Crimes Act 1961

²⁴ At 540.

appeared to make no provision for mistake at all, others seem to have required reasonable mistakes.

In 1979 the Criminal Law Reform Committee was asked to review the self-defence provisions. The Committee proposed the removal of the distinction between provoked and unprovoked assaults and the introduction of a wholly subjective standard (honest belief standard) for the defender's beliefs.²⁵ The reason for the first of these changes was clear: simplification. The reason for the adoption of the honest belief standard is less clear. The Committee itself gave no reasons for its recommendation and when the amendment to the Crimes Act was debated in Parliament the Minister of Justice did not seek to justify the change. There appears to have been concern that it might result in unmeritorious claims, since the Minister pointed out that claims to have held wholly unreasonable beliefs would quite probably not be credible²⁶ and Geoffrey Palmer, for the Opposition, expressed some concern about "cases involving mantraps or spring-guns".²⁷ However, neither Government nor Opposition regarded this as a matter worth serious debate.

The explanation of the change to an honest belief test can be found, however, by looking at the Committee's general approach to criminal law. The Criminal Law Reform Committee has been described as having "pursued a consistently subjectivist approach to criminal liability".²⁸

The basis of subjectivism is the idea that *mens rea* for a criminal offence should be either intent or recklessness; negligence is insufficient (unless a statutory definition of an offence refers specifically to negligence). If a subjectivist approach is taken to criminal liability, a person who has done a *prima facie* criminal act under the influence of an unreasonable mistake of fact will not be liable. She may have been negligent in making the mistake but that is insufficient to justify punishment for an offence that requires intention or recklessness. In order to achieve a result intentionally it is necessary to have that result in mind; the mistake shows that the actor had a different result in mind and did not do the unlawful act intentionally. Recklessness involves awareness of a risk of causing a result; again, the mistake cancels out the recklessness.

²⁵ Criminal Law Reform Committee, *Report on Self-Defence* (1979).

²⁶ NZPD 1 August 1980, 2284.

²⁷ *Ibid*, 2285.

²⁸ Hannan, "Pragmatism and Principle in the Construction of Change: The Criminal Law Reform Committee" (1988) 13 NZULR 206, 209.

This approach to liability lies behind an argument made by Smith and Hogan in the third edition of *Criminal Law*, published in 1973:

An unreasonable mistake is negligence. It is therefore submitted that if D has killed, in the belief, arising from an unreasonable mistake of fact, that it was necessary to do so to prevent crime or in self-defence, he should be convicted of manslaughter, if his mistake was a grossly unreasonable one. Unless his mistake could be said to amount to gross negligence, he should have a complete defence.²⁹

To deny self-defence to a person who had made an unreasonable mistake was contrary to (subjectivist) principles of criminal liability.

In 1975 an argument like this was accepted by the House of Lords in relation to rape. In *DPP v Morgan*, the defence was that the defendants believed that the complainant was consenting to intercourse. The jury convicted after being instructed that this was a defence only if the mistake was reasonable. The House of Lords decided that this was a misdirection. Rape could not be committed negligently, it involved having intercourse "recklessly and not caring whether the victim be a consenting party or not".³⁰ Any belief that the complainant consented, however unreasonable, was inconsistent with an intent to have intercourse with someone who was not consenting or with recklessness about her consent.³¹

The decision in *Morgan* was controversial, and the New Zealand legislature amended the Crimes Act 1961 to ensure that liability extended to those who made unreasonable mistakes about consent.³² However, the Criminal Law Reform Committee had already prepared a report on the decision in *Morgan* that endorsed the House of Lords' reasoning:

They quoted with approval a passage from Glanville Williams to the effect that the test of intention is subjective, not objective...The Committee concluded that if criminal liability is, properly, based on subjective principles, then an unreasonable mistake must negate liability...And the Committee specifically rejected the

²⁹ Smith, JC and Hogan, B, *Criminal Law* (3rd ed, 1973), 263.

³⁰ *Morgan v DPP* [1975] 2 All ER 347, 357.

³¹ The appeal failed, however, because there was insufficient evidence that the appellants had honestly believed that the complainant consented.

³² Crimes Act 1961 s128(2) and (3) sets out the *mens rea* for the offence of sexual violation.

suggestion of a lesser offence of rape by negligence, for the reason that it felt that negligence should not, generally, be the test of criminal liability.³³

The House of Lords limited its reasoning in *Morgan* to rape but some academic commentators disagreed. Honest mistake would also negate the *mens rea* for offences of violence if it meant that the actor believed that she was acting in self-defence and the force used would have been reasonable had her interpretation of the circumstances been correct. She did not intend to act unlawfully because it is not unlawful to use reasonable force in self-defence.³⁴ In 1975 Ashworth wrote:

Since ... even an unreasonable mistake negatives the element of knowledge which is an essential component of criminal liability, a purely subjective test should likewise apply to a person's belief in the circumstances of necessity upon which a justificatory defence might be based". [This argument applied both to a] person who (mistakenly) believes that someone is about to attack him, or that there is no safe avenue of withdrawal .³⁵

Editions of Smith and Hogan and Glanville Williams appearing after the decision in *Morgan* took the same view.³⁶

Direct evidence that arguments like these persuaded the Criminal Law Reform Committee to recommend an honest belief test is hard to find. There are references to a codification proposal from the British Criminal Law Revision Committee that omitted to include a reasonable belief component,³⁷ and to an article by Griew discussing those proposals. Griew

³³ Hannan, *supra* note 28, 209, referring to Criminal Law Reform Committee, *The Decision in DPP v Morgan: Aspects of the Law of Rape* (1980).

³⁴ This assumed a particular explanation of how self-defence operates as a defence. Rather than being a supervening defence, coming into operation notwithstanding that both *actus reus* and *mens rea* of an offence had been proved, it qualified the *mens rea* for offences of personal violence. The intent must be to use unlawful force not simply to use force.

³⁵ Ashworth, "Self-Defence and the Right to Life" [1975] *Camb LJ* 282, 304-305. Emphasis added.

³⁶ Smith, JC and Hogan, B, *Criminal Law* (4th ed, 1978) 329; Williams, G *Textbook of Criminal Law* (1978) 452. The post-*Morgan* argument was basically no different from the one described in the earlier edition of Smith and Hogan, but its structure made it more attractive to courts since it could be accepted on an offence/defence by offence/defence basis without any need for philosophical discussion about the nature of *mens rea*.

³⁷ Criminal Law Reform Committee, *supra* note 25, at 7, quoting para 166 of the English report.

expressed a preference for a wholly subjective test - but gave no reasons for this preference.³⁸ The published words of the Committee provide no further clues about its reasoning. Perhaps this is the most cogent evidence in favour of its acceptance of the approach described above. If the Committee had reached the same conclusion as the English academics, but for different reasons, it seems likely that it would have explained itself.

It is therefore submitted that the reason New Zealand adopted an honest belief standard for self-defence in 1980 was the view that the reasonable belief standard was contrary to principles of criminal responsibility.³⁹ The subjectivist approach that was rejected for the offence of sexual violation triumphed in the defence of self-defence.

IV. THE CORRECT INTERPRETATION OF “THE CIRCUMSTANCES AS SHE BELIEVED THEM TO BE”

The difficulty with section 48 is one of statutory interpretation. The New Zealand approach to such problems can be summarised as follows:

...courts are to apply that which they take to be the intended meaning of a statutory provision so long as it is a possible meaning of the language used...In deciding what is a possible meaning the courts should rely on their understanding of the conventions governing the ordinary use of language. To decide what was the intended meaning of a provision they should take account of what appears to be its purpose, as well as of any other indications of its meaning available to them.⁴⁰

An analysis of the words of section 48 together with its supposed purpose suggests that the correct approach to the section is the one that has been labelled the “broad” approach.

The starting point in determining the meaning of section 48 is to look at the meaning of the words themselves. There is a potential difficulty with relying upon notions of legislative intent. When enacting section 48, the legislature almost certainly did not give thought to the precise meaning of “the circumstances”. Is the legislative intent limited by the meaning the legislators had in mind at the time of enactment? Payne argued that it should

³⁸ Griew, “Non-Fatal Offences and Self-Defence” [1977] Crim LR 91, 99.

³⁹ The English courts themselves later adopted an honest belief test for self-defence, relying on the defender’s lack of mens rea. See *R v Williams* [1987] 3 All ER 411.

⁴⁰ Evans, PJ *Statutory Interpretation: Problems of Communication* (1988) 2. Although the Acts Interpretation Act 1924 governs the general approach to statutory interpretation in New Zealand, it does not change common law doctrine.

be and that “it would ... be a strange use of language to say that the user of a general word 'intends' it to apply to a particular that never occurred to his mind”.⁴¹ MacCallum convincingly argued that intent can cover such cases:

I might react against the claim that I had intended x by making statements roughly in the form: ‘The thought of such a thing as x never occurred to me’. But the point of this remark is not merely that the thought of such a thing as x had not occurred to me; there is also a clear suggestion that if such a thought had occurred to me I would have excepted such things as x. Without this further suggestion, my remark would surely seem pointless.⁴²

It is not known what examples were to the fore of the legislators' minds when enacting section 48, but there is no reason why the operation of the section should be limited to the types of case that were actually anticipated. If the further types of case are within the permissible meanings of the words used and they also come within the reasons for the rule, the legislative oversight does not matter.

The important words are “belief” and “circumstances”. The *New Shorter Oxford English Dictionary* defines a belief as “mental acceptance of a statement, fact, doctrine, thing, etc, as true or existing”. To believe something is to “accept the truth or reality” of it, to “hold as true the existence of” it or to “think or suppose (someone or something) to be..”. A circumstance is “that which stands around or surrounds”, or “the material, logical or other environmental conditions of an act or event; the time, place, manner, cause, occasion, etc, of an act or event; the external conditions affecting or that might affect action”.⁴³

When the phrase “the circumstances as she believed them to be” is read with the rest of section 48, these definitions provide an indication of the content of beliefs about circumstances. The subjective test modifies the objective test where a mistake about a “circumstance” has been made. It cannot do this unless the content of the belief is logically related to the reasonableness of the believer's defensive response. It must be something the truth or existence of which is relevant to an assessment of the reasonableness of the defender's actions: in effect it must be a belief about an external condition that affects or might affect action.

⁴¹ Payne, “The Intention of the Legislature in the Interpretation of Statutes” (1956) 9 *Current Legal Problems* 96, quoted by Evans, *supra* note 40, 187.

⁴² MacCallum Jun, “Legislative Intent” in Summers, R S *Essays in Legal Philosophy* (1968), quoted by Evans, *supra* note 40, 188.

⁴³ *New Shorter Oxford English Dictionary* (1993).

The type of relationship this requires is shown by looking at the effect of a mistake about the nature of a threat. If Carlos is attacked by Derek, Carlos' belief that Derek is armed is relevant to the reasonableness of Carlos' response. Assuming that Carlos is roughly the same size as Derek, and has some fighting skills, it is probably unreasonable for him to use a weapon to defend himself: it is unnecessary because he can use his hands and it is disproportionate because a weapon will cause much greater injury than the unarmed Derek could inflict with his hands. It is very different if Derek is armed: he can inflict much more harm, and it is less likely that bare hands will repel the assault. Carlos' belief about whether Derek is armed is a belief about an external condition that, if true, would impact upon the reasonableness of the defender's response and hence a belief about "the circumstances".

This interpretation of the test does not provide grounds for limiting beliefs about the circumstances to beliefs about the mode of attack, as a further hypothetical example demonstrates. Angela is alone with Brendan in an isolated property. Brendan threatens to kill Angela in the morning and then goes to bed. Angela believes that the telephone has been cut off, and Brendan has told her that he has disabled the car to stop her from running away. He is lying but Angela believes him and concludes that she has no means of escape from the house. During the night, she shoots Brendan. If Angela's belief that she was effectively trapped was correct, it might be reasonable for her to use force while Brendan was sleeping. On the other hand, if she did not believe that she was trapped, it would almost certainly be unreasonable for her to use that force: she would be expected to use the car or telephone to get help. The options available to Angela are logically related to the reasonableness of her response to Brendan's threats, and therefore her beliefs about those options are beliefs about the circumstances for the purposes of section 48.⁴⁴

The test described here is not concerned with the reasonableness of the belief in question. Where a belief relates to the nature of a threat, reasonableness is relevant only to credibility; this is true whatever the subject matter of the belief. Section 48 would appear to allow self-defence to be put to a jury even where the defendant's beliefs stemmed from an insane

⁴⁴ This is not to say that Angela *was* reasonable to kill Brendan while he was asleep. Even once Angela's belief that the car was disabled was taken into account, her use of force might be unreasonable: there may have been some other alternative that she did not consider. It might be unreasonable by definition to kill someone who is asleep, whatever options for escape are available. The crucial point is that her belief is a relevant one.

delusion.⁴⁵ If Angela believed that the car was out of order because it had been attacked by aliens, the logical relationship between her belief and her subsequent actions would be unchanged: it would still be a belief about “the circumstances”.

The dictionary meaning of relevant words therefore appears to support a broad reading of the phrase “the circumstances as she believed them to be”. The narrower interpretation of the phrase requires different mistakes of fact to be treated differently but there is nothing in the words used to justify the distinction between different kinds of mistakes which is the effective result of cases such as *Jenkins* and *Wang*. On this reasoning, it would seem that the approach in *Crowe* is the correct one.

However, it is obviously not impossible that the phrase could be interpreted in the narrow way. If the broad interpretation is inconsistent with the reasons for the use of the subjective test, it may be necessary to return to the narrower meaning. It was submitted above that the basis of the honest belief test is the view that a person who believes that she is acting in self-defence lacks the *mens rea* for a crime of personal violence. What she *intended* to do was not an offence because it is not unlawful to use reasonable force in self-defence, even if that force is used intentionally. Therefore she did not commit the offence intentionally and she should not be subject to punishment despite the consequences of what she did.

This argument seems to apply equally well to beliefs about all aspects of the circumstances of a self-defence claim. In the Angela and Brendan hypothetical example, Angela held a positive belief that she had access to neither car nor telephone. What the law really required in the circumstances was that she use a non-violent method of protecting herself; her mistake meant that she did not have “normal capacities ... for doing what the law requires and abstaining from what it forbids, and a fair opportunity to exercise these capacities”.⁴⁶ She was unaware of the opportunity to use a non-violent method of protecting herself.

The argument is basically the same as that which applies when a mistake is made about the nature of a threat. The law demands that a person who is attacked by someone who is unarmed resists using a weapon if she is capable of protecting herself without one or if the attack will cause her no real harm. But she does not have a fair opportunity to comply with this

⁴⁵ *R v Green* (1993) 9 CRNZ 523 (CA).

⁴⁶ Hart, “Negligence, Mens Rea and Criminal Responsibility” in Hart, HLA *Punishment and Responsibility* (1968) 152.

demand if she believes, mistakenly, that her attacker is armed. If a defender reacts in a way that would be appropriate if she was correct about the facts, it is not appropriate to treat her as if she had not made that mistake.

The case of *R v Wang* was considered earlier in this article as an example of a court ignoring a defender's beliefs about the possibility of escape. Given the facts as stated in the Court of Appeal's decision, it is not possible to state whether the outcome would have been different if section 48 was interpreted broadly. It is unclear what Wang actually believed: this might have been a case in which the defendant failed to think about what options were available to her and simply did the first thing that came to her mind. Or she might wrongly have thought that she had considered all the options but omitted to consider the possibility of escape or asking for help. Alternatively, she may have considered the possibility of escaping or contacting the police or others for help and rejected these options. The outcome of her self-defence claim would not be the same in all these scenarios.

The disadvantage of this interpretation of section 48 is that there is a risk that it could dilute the objective test. In most of the examples discussed so far, the matters upon which the actors were mistaken allowed for the normal operation of the objective test. The result of the self-defence claim still depends on careful application of the reasonable force test. A defender must take the care that a reasonable person would take and this will sometimes involve considering something that the defender failed to consider. All that the subjective test demands is that, if the defender holds a belief about a circumstance, she must be treated as if the belief was correct, but this does not mean that she must be treated as if the only matters to be considered were those which she actually considered. The failure to think about something is not holding a belief about that thing. Because these further factors will be taken into account when the reasonableness of actions is judged, the objective test remains meaningful.

A serious problem would arise if a defender wrongly believes that she has considered all the alternatives to force: can this be described as a belief about the circumstances? It seems to satisfy the test described earlier, but the effect of fixing the circumstances by the belief is to limit severely the operation of the objective test. The defendant would have to be treated as if she had considered all the alternatives, even if she had omitted some, and her response to the danger would be certain to be judged reasonable. A belief that "this degree of force is reasonable" is easily excluded from beliefs about the circumstances, because including it would not work within

the structure of section 48; the belief that all options have been considered is less easily excluded.

One answer would be to try to distinguish between beliefs about verifiable material facts - for example, that a telephone was broken - and conclusions based upon those beliefs, and to deny that the latter were really "beliefs" in the strict sense. This would be extremely complicated, though, because even the initial belief about the telephone would turn out to be a conclusion based on other facts. The solution to the problem probably lies in the legislature's intention. The inclusion of an objective test in section 48 signalled that it was not for a defender to decide for herself what it would be lawful to do. Any belief that effectively takes that decision away from the judge or jury is outside the intended scope of the words of the section. This might be a qualification based on policy or it might be justified on the ground that such a belief is not a belief about an external condition that affects or might affect action.

In *Wang*, the trial judge referred to "a return to the law of the jungle" and the Appeal Court quoted (indirectly) from the decision in *Jahnke v State*, where the judge complained about a "leap into the abyss of anarchy".⁴⁷ Finn sees this as a concern about the potential for dilution of the objective component of the defence and suggests that there is a covert policy decision being made in *Wang* to exclude certain types of mistaken belief from the ambit of section 48.⁴⁸ It has been demonstrated in this article that this concern about the objective element of section 48 is misplaced. The objective test is capable of operating as it was intended to operate.

V. CONCLUSION

This article has argued that the phrase "the circumstances as she believes them to be" requires courts to take any material mistakes of fact into account when deciding whether a person's actions were reasonable. These may include mistakes about whether a particular alternative to using force was available. The only limit to what can be a belief about circumstances is that the belief has to be about something that is logically connected to the objective reasonableness of force. If the effect of treating the mistaken belief as correct is to deny any real operation to the objective reasonableness, that belief is not within the scope of the circumstances as the defender believes them to be.

⁴⁷ *Jahnke v State* 682 P 2d 991, 997 (Wyo 1984) quoted in *R v Wang* [1989] 3 NZLR 529, 538.

⁴⁸ Finn, Case note on *R v Wang* (1990) 14 Crim LJ 200, 203.

In most cases, it would make little difference if section 48 was interpreted in this way rather than in the way it is at present. Many uses of excessive force are the result of panic rather than mistake, and the proposed reinterpretation would make no difference to the outcome of these cases. In most cases where a mistake really has been made, the defender is already treated as if the circumstances were as she believed them to be, either because of the subject matter of her mistake or because it was reasonable. The impact of the proposed reinterpretation of section 48 arises in cases like *Wang* “where ... the defendant perceives his or her situation in a way which is different from the way an ordinary person would perceive it.”⁴⁹ At present, in such cases there is a risk that the court will decide that there is no credible narrative of self-defence, and the defence will not even be put to the jury. The broader interpretation of section 48 makes it more likely that juries will have the opportunity to consider the actions of the defendant in light of her own, fully explained, view of the circumstances. This could be particularly valuable in cases involving abused women, where their previous experiences of violence and of the assistance available to them might lead to a view of the circumstances which differs from that which a person without those experiences would form. It is true that such experiences may be revealed in the course of the evidence in any case, but the proposed interpretation of section 48 makes it much clearer why and how they are relevant to the self-defence claim.

The cases that really concern the judges seem to be those where the defendant's view of the circumstances is wholly unreasonable. If a defendant's assertion is that the police would not assist her because she had heard a rumour they did not respond to domestic incidents or that she did not go to a neighbour because they had had an argument earlier and she did not think the neighbour would help her, there would indeed be an extension of self-defence to some doubtful cases. Should someone who resorts to force on the basis of such flimsy fact-checking be acquitted? This problem is a real one but it is not unique to mistakes about opportunities for escape: exactly the same problem arises with mistakes about other aspects of the circumstances. As section 48 is currently applied, there is no reason why self-defence should be denied to a person whose ground for believing another person is a threat to her is that person's ethnicity. This application of the defence is at least as morally doubtful as the application in the cases referred to above. The reason why these cases are unmeritorious is that the mistakes demonstrate a blameworthy lack of respect for other people. The Court of Appeal is right to stress “society's concern for the sanctity of

⁴⁹ *Ibid*, 202.

human life”.⁵⁰ but the solution lies in careful consideration of the honest belief test itself. There is no legitimate ground for distinguishing between blameworthy and blameless mistakes within the words of section 48. Concern about the scope of self-defence would be better directed towards a re-examination of this aspect of section 48.

⁵⁰ *R v Wang* [1989] 3 NZLR 529, 539.

CASE NOTE

FORTEX GROUP LTD (In Receivership and Liquidation) v MACINTOSH

BY RUTH WILSON*

I. INTRODUCTION

*Fortex Group Ltd (In Receivership and Liquidation) v MacIntosh*¹ is a recent decision of a five member Court of Appeal² which puts in question the future role of the remedial constructive trust in New Zealand. Prior to this decision it could have been safely assumed that the remedial constructive trust was part of the New Zealand judicial armoury, but now this assumption has been put on the agenda for further consideration.

As Tipping J emphasised, the case before the Court did not require any final decision whether the distinction between institutional and remedial constructive trusts³ is a helpful one, or any closer analysis of the underlying concepts, or even a decision “whether the so-called remedial constructive trust should be confirmed as part of New Zealand Law”. These matters, now

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¹ [1998] 3 NZLR 171.

² The result was unanimous. Tipping J delivered the leading judgment on behalf of himself, Gault and Keith JJ, with individual judgments delivered by Henry and Blanchard JJ. Henry J agreed with the conclusions and reasons contained in the joint judgment regarding the express and institutional constructive trust, but approached the remedial constructive trust differently; and Blanchard J agreed both with the joint judgment and Henry J's observations.

³ The remedial constructive trust, along with the express and institutional trust, were defined for the purpose of the case: “An express trust is one which is deliberately established and which the trustee deliberately accepts. An institutional constructive trust is one which arises by operation of the principles of equity and whose existence the Court simply recognises in a declaratory way. A remedial constructive trust is one which is imposed by the Court as a remedy in circumstances where, before the order of the Court, no trust of any kind existed. The difference between the two types of constructive trust, institutional and remedial, is that an institutional constructive trust arises upon the happening of the events which bring it into being. Its existence is not dependant on any order of the Court. Such order simply recognises that it came into being at the earlier time and provides for its implementation in whatever way is appropriate. A remedial constructive trust depends for its very existence on the order of the Court; such order being creative rather than simply confirmatory” (supra note 1, at 172-173).

signposted for future judicial consideration, have been left to “await another case in which those issues necessarily arise”.⁴

However, despite the overall impression that this decision takes away more than it gives, it does contain some guidance for future cases. In particular the joint judgment:

- articulates unconscionability as a single foundational principle to explain or justify the imposition of both types of constructive trust;
- clarifies the unconscionability principle so as to recognise the position of any third party who has an interest in the property that would be affected by the imposition of a remedial constructive trust. It is the conscience of the latter party, not the original wrongdoer’s conscience, that is relevant;
- recognises that there may be occasions where a proprietary remedy “such as the so-called remedial constructive trust”, would be a useful weapon in equity’s armoury;
- counsels against varying settled insolvency rules on too loose a basis by according priority via a remedial constructive trust;
- clarifies the need for subject matter in the form of a separately identifiable fund for express and institutional constructive trusts;
- confirms that the extended notion of tracing suggested in *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd*⁵ is limited to cases of express or institutional constructive trusts and is of no assistance where money has been paid into an overdrawn account.

This note will describe the decision, compare it with the law as previously understood, and comment on the changes it may herald. It will conclude that, given the potential of the remedial constructive trust to re-order proprietary rights, the current uncertainty as to its doctrinal underpinning is undesirable. It will suggest that the Court of Appeal is putting the profession on notice that if this trust is to remain part of our law the underlying concepts require further analysis.

II. THE DECISION

1. *The facts and issues*

The plaintiffs were employees of the Fortex group of companies and members of the company’s two superannuation schemes. The two funds (for

⁴ *Supra* note 1, at 173.

⁵ [1986] 1 WLR 1072.

management and non-management employees respectively) had been established by trust deeds in similar terms and imposed similar obligations on Fortex Group Ltd (which was both participating employer and the trustee of the fund established under the scheme). Both funds involved contributions made by the employees (by way of deduction from their salaries and wages) supplemented by contributions from Fortex. The trust deeds required all contributions to be made to the trustee monthly.

On Fortex's collapse it emerged that, although journal entries had been made by Fortex regarding the funds, the company had adopted the practice of paying the total contributions to the management fund on an annual basis. No separate fund had been set up in respect of the unpaid contributions prior to the intended annual payment to the scheme manager. When receivership supervened, payments from the previous year were outstanding. Fortex had, however, until shortly before receivership, made fortnightly payments to the staff fund. Once the priority accorded to employees under section 308 of the Companies Act 1993 was taken into account, the management fund and the staff fund were owed \$257, 592.45 and \$45, 830.55 respectively.

It also emerged that, if Fortex's accounts were looked at on a consolidated basis, the company had been in overdraft throughout the relevant period.

In these circumstances the plaintiffs, having obtained summary judgment against Fortex for breach of contract and breach of trust, sought priority ahead of the secured and unsecured creditors by seeking a declaration that Fortex held the relevant sums on either an express or constructive trust, or that they were entitled to a restitutory proprietary interest in the form of a remedial constructive trust.

In the High Court Gallen J dismissed the claims to an express trust and a constructive trust on the basis that there was no identifiable trust property. However, he upheld the remedial constructive trust claim.⁶

Fortex and the trustee for the group's secured debenture stockholders appealed. The management scheme employees cross-appealed from the judge's rejection of their claim to an express or institutional constructive trust. The appeal was allowed and the cross-appeal dismissed. The employees were relegated to the status of unsecured creditors.

⁶ *MacIntosh v Fortex Group Ltd* (1997) 6 NZBLC 102,141.

2. *The subject matter issue - express and institutional constructive trusts*

Gallen J applied the third of Lord Browne-Wilkinson's fundamental trust law propositions identified in *Westdeutsche Landesbank Girozentrale v Islington Borough Council*:⁷ "[i]n order to establish a trust there must be identifiable trust property".⁸

The plaintiffs' alleged trust property consisted of "contributions by way of deduction which they never received and which were never in fact paid to anybody and contributions which Fortex was contractually bound to make, but which were never paid".⁹ The defendants argued that the journal entries did not transfer funds, but merely reflected contractual arrangements without conferring proprietary rights sufficient to enable the funds to be traced.

Gallen J accepted "that Fortex must be deemed to have *identified for trust purposes*, at least those sums which would have represented the contributions of the plaintiffs to the fund as having been deducted from their salaries and wages" (emphasis added). However he held that, as Fortex's account was always overdrawn, "no sum was ever set aside which the plaintiffs could now claim *remained identified* by a trust attached to it".¹⁰ He relied on the English Court of Appeal decision in *Bishopsgate Investment Management Limited (in liq) v Homan*,¹¹ which held that equitable tracing, though designed for the protection of trust money misapplied, cannot be pursued through an overdrawn and therefore non-existent fund. The constructive trust claim also foundered for much the same reason.

On appeal, Tipping J upheld Gallen J's conclusions but on the basis that "the retained moneys were never separately identifiable *as a fund* in themselves", and that "at no time was there any *separately identifiable fund* in respect of which Fortex can be regarded as having become a constructive trustee for the plaintiffs".¹² If this was so, and there never was any identifiable trust

⁷ [1996] 2 All ER 961, 988. Lord Browne-Wilkinson's "Identifiable Trust Property Principle" is discussed at pp 87ff of this Review. On appeal, Lord Browne-Wilkinson's third trust principle was not specifically discussed but the reasoning in the joint judgment in *Fortex* is consistent with the interpretation of that principle in the above article.

⁸ (1997) 6 NZBLC 102,141, 102,146.

⁹ At 102,146.

¹⁰ At 102,147.

¹¹ [1995] 1 All ER 347.

¹² [1998] 3 NZLR 171, 174-175 (emphasis added).

fund, it was not necessary to consider the further question of whether that fund was traceable (that is, had *remained* identifiable). Therefore the overdrawn account was not relevant. Nonetheless, the joint judgment addressed this issue: “when the retained moneys were effectively retained in, or paid into an overdrawn bank account, *they either never had, or ceased to have, any separate identity*”.¹³ In actual fact there were no retained moneys but, this aside, the reference to the overdraft raises the question of what would have happened if the account had been in credit.

3. *The remedial constructive trusts issue*

In the High Court, Galleen J, using terms not entirely familiar to all practitioners, recognised “a restitutionary proprietary interest by way of a remedial constructive trust on the ground of unjust enrichment”. The following points are made as background to the discussion in *Fortex*.

Restitution is a remedial response available in two dimensions.¹⁴ First, it is the sole remedial response to all those cases where the cause of action or basis of liability is unjust enrichment. If a plaintiff can show a basis of unjust enrichment, “the defendant has a restitutionary duty, so named because the content of her duty is the transfer back of wealth received”.¹⁵ In these so called autonomous unjust enrichment cases, both the cause of action and the remedial response belong to the law of restitution. The defendant must make restitution because she has been enriched. Liability is strict (that is, not conscience-based) subject to defences.

Secondly, the response of restitution may be available in cases where liability is based not on unjust enrichment but on some other duty arising in tort, equity or contract. These so-called “restitution for wrongs cases” are concerned with defining the circumstances in which the plaintiff can claim a gain from the defendant received as a result of the defendant’s wrongdoing. Where equitable wrongs are involved, liability is conscience-based. These cases are relevant to the law of restitutionary responses, but they are not part of it. Restitutionary responses (remedies) are part of the law of restitution.¹⁶

In cases of autonomous unjust enrichment, the plaintiff must establish (i) an enrichment of the defendant that is (ii) at the expense of the plaintiff and that

¹³ *Supra* n 1 at 5 (emphasis added).

¹⁴ Rickett, C and Goddard, D *NZLS Seminar - Developments in the Law of Obligations - Tort, Equitable Duties and the Effect of Contractual Relationships* (1996) 8.

¹⁵ *Ibid*, 6.

¹⁶ Rickett and Goddard, *supra* note 14, at 9.

(iii) the enrichment is unjust.¹⁷ There is no need to establish unjust enrichment in cases involving restitution for wrongs. However, some cases are susceptible to analysis in both the categories. Indeed, although the above distinction between the two types of case was not drawn in *Fortex*, Gallen J appears to have regarded the case as one of autonomous unjust enrichment. The joint judgment in the Court of Appeal approached the case from the perspective of equitable wrongdoing. Henry J took both approaches.

As *Fortex* illustrates, where insolvency is involved, the restitutionary claimant will seek a proprietary restitutionary response, not a personal one. A *restitutionary proprietary* claim is made by a plaintiff alleging that certain property *ought to be* hers in contrast to a *pure* proprietary claim in which she alleges that the property *is* hers. If granted, this may enable the plaintiff to relief in priority to secured and unsecured creditors of the insolvent party who received the gain from the plaintiff. The court may respond to a restitutionary proprietary claim by imposing a remedial constructive trust, thereby creating property rights in the claimant where none previously existed.

The doctrinal basis on which the courts in America and Canada will impose such a remedy is unjust enrichment. On the other hand, New Zealand courts have tended to see the remedial constructive trust broadly as a device to redress unconscionability.¹⁸ Accordingly, Gallen J's decision could be seen as an attempt to move towards the North American approach to the imposition of the constructive trust.

On the question of unjust enrichment, His Honour reasoned that, although no monetary enrichment was received by *Fortex*, the company obtained an advantage in that it avoided paying interest on an increased overdraft, and it freed up for general purposes funds which it was under a fiduciary obligation to use for the benefit of the plaintiffs. These factors provided "at least an element of unjust enrichment".¹⁹ As to the first factor, as Henry J would later point out, the enrichment would be the interest "saved" on the unpaid contributions not the unpaid contributions themselves. As to the second factor, there were no funds to which any fiduciary obligation had attached.

Next, His Honour turned to "unconscionable behaviour or unconscionality", not as an alternative basis for the imposition of a remedial constructive trust

¹⁷ *Ibid*, 4.

¹⁸ Fardell and Fulton, "Constructive trusts - A new era" [1991] NZLJ 90.

¹⁹ (1997) 6 NZBLC 102,141, 102,149.

but to decide “was there any enrichment and was that enrichment unjust”.²⁰ It is difficult to see how this would assist in determining the first question. Nonetheless, His Honour held that there was “a degree of enrichment” and that enrichment was unjust because of Fortex’s fiduciary obligations and the employer/employee relationship.

He concluded in a passage which would later be quoted by the Court of Appeal:

Looked at overall, Fortex clearly gained an advantage because it did not carry out the obligations which were imposed upon it. That involves a degree of unjust enrichment.

I am satisfied that Fortex gained an advantage sufficient to justify the intervention of the Courts if in other respects that intervention is appropriate. I am satisfied also that the necessary grounds of conscience which justify equitable intervention, have been established and arise substantially because of the nature of the relationship between the parties, the nature of the obligation which existed, the recognition and part performance of it and the effect on the plaintiffs.²¹

In the Court of Appeal Tipping J selected unconscionability as the “principled basis” for declaring that assets owned in law by A should be held by way of remedy in trust for B both *vis a vis* A and any other person with an interest in the property which would be affected by the imposition of the trust :

Equity intervenes to prevent those with rights at law from enforcing those rights when in the eyes of equity it would be unconscionable for them to do so.²²

As all Fortex’s assets would be required to satisfy the indebtedness secured by the debenture, only the secured creditors had any legal rights to them. Accordingly, the plaintiffs could establish a remedial constructive trust only if they could “point to something which can be said to make it unconscionable - contrary to good conscience - for the secured creditors to rely on their rights at law”. Tipping J examined the “necessary grounds of conscience” identified in the court below and concluded that Gallen J seemed to have been looking at Fortex’s conscience rather than that of the

²⁰ At 102, 150.

²¹ At 102,150.

²² [1998] 3 NZLR 171, 175.

secured creditors. This was incorrect as “[i]t is of course, the conscience of the secured creditors which is crucial in this case”.²³

The claimants’ argument that the conscience of the secured creditors was irrelevant, in that there was no need to say that their conscience was in any way affected, was firmly rejected by Tipping J, along with an alternative argument that there was an element of unjust enrichment which should affect the secured creditors’ conscience.²⁴

This latter argument was dealt with very briefly probably because Tipping J felt it inappropriate to regard the secured creditors as having been enriched at all, let alone unjustly so. Nonetheless, the Court seemed to think that if there had been enrichment the secured creditors were entitled to it on the basis of their security granted in return for advancing money to the company. This seems to involve a determination of the unjust enrichment question as between the company and the secured creditors rather than between the secured creditors and the claimants, and as such is inconsistent with the approach to the unconscionability argument.

Finally, counsel for the claimants argued (without specifying whether this argument was by way of analogy to unjust enrichment or was raised in connection with unconscionability) that the value of the money was “latent” in Fortex’s general assets. The decision in *Space Investments*²⁵ and the *Gillies v Keogh*²⁶ line of cases formed the basis of this argument. Although Tipping J incorrectly summarised the outcome in the first case and again referred to “the retained moneys” as if they really existed, he effectively quashed any notion that the extended notion of tracing suggested in the *obiter* in *Space Investments* might have any application to remedial constructive trust cases or was of assistance where money had been paid into an overdrawn account.

The *Gillies v Keogh* line of cases was distinguished:

The constructive trust which arises in de facto matrimonial property cases is of an institutional, rather than remedial kind. That is an immediate point of distinction.

²³ At 176. Henry J concurred in general terms with the joint judgment’s treatment of the unconscionability point.

²⁴ At 177: “We cannot accept that proposition, which flies in the face of the whole basis upon which equity intervenes to restrain reliance on rights at law”.

²⁵ *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Company (Bahamas) Ltd and Ors* [1986] 3 All ER 75.

²⁶ [1989] 2 NZLR 327.

Furthermore, the constructive trust which arises in such cases is itself conscience based.

...[this] line of cases serves to confirm the need for the conscience of the secured creditors in the present case to be affected.²⁷

As well as indicating a single foundational principle for both types of constructive trust, this passage preserves the distinction between them.

The joint judgment ended, on the same note as it had opened, by stressing the unsettled position of the remedial constructive trust. The link between the defendant's insolvency and the plaintiff's desire for a proprietary remedy was referred to, along with the potential for third party rights to be affected:

If the plaintiff wishes to gain priority over those who would otherwise be entitled to the defendant's assets, the court must be careful not to vary settled insolvency rules on too loose a basis. That said, there may be occasions, in the present field or others, when a proprietary remedy, such as the so-called remedial constructive trust, would be a useful weapon in equity's armoury.²⁸

4. The subject matter or identifiability issue for remedial constructive trusts

In the High Court Gallen J held that in an appropriate case a court exercising its general equitable jurisdiction could attach a trust to other assets otherwise unassociated with the particular claim.²⁹

On appeal Tipping J required only "some asset or assets in the defendant's hands in respect of which the Court considers it to be appropriate to impress a trust in favour of the plaintiffs". However, Henry J regarded the absence of any separate and identifiable fund to which the employees could lay a claim "as a fundamental objection to the imposition of a trust".³⁰

III. COMMENTARY

1. Continued availability of the remedial constructive trust in New Zealand?

Taken at face value, this important decision reflects a significant retreat from the Court of Appeal's endorsement of the remedial constructive trust in

²⁷ [1998] 3 NZLR 171, 178.

²⁸ At 179.

²⁹ (1997) 6 NZBLC 102,141, 102,150.

³⁰ [1998] 3 NZLR 171, 175, 180.

the last decade. First granted within the context of de facto property disputes, the Court indicated in its 1989 decision in *Elders Pastoral Ltd v Bank of New Zealand*³¹ that it was prepared to make the remedy widely available. Although the Privy Council reversed the decision on another ground, their Lordships did not deal with the constructive trust issue and it would seem that the Court of Appeal's findings thereon remained authoritative.

In 1992 the availability of the remedial constructive trust went unquestioned by Gault and McKay JJ in *Liggett v Kensington*.³² On the facts of the case, Gault J was prepared to impose such a trust, McKay J was not and Cooke J preferred an alternative approach.

When the case went to the Privy Council as *Re Goldcorp Exchange Ltd (In Receivership) : Kensington v Liggett*³³ Lord Mustill, discussing whether the Court *should* create a remedial restitutionary right after the event which would take priority over the secured creditor, far from suggesting that it *could* never do so, indicated that in appropriate factual circumstances remedial restitutionary rights "may prove to be a valuable instrument of justice" in what he had previously described as "this important new branch of the law".³⁴

Against this background, and the final conclusion in *Fortex* as to the usefulness of the remedy "in all types of case", the decision in this case cannot be regarded as an outright rejection of the remedial constructive trust in New Zealand. Furthermore it is, with the greatest respect, difficult to accept that the court's power to impose such a trust is uncertain or in need of confirmation. No authority was cited in support of the reservations voiced in the joint judgment. Henry J, while noting that the concept "has not been sufficiently developed" since its uncertainties were noted in *Goldcorp*, did not question its availability. Blanchard J preferred to leave the question to another day.

It is submitted that what really concerned the Court was not the availability of the remedy as much as the need to establish a principled basis on which it may be invoked and some criteria to guide the Court in exercising its discretion whether to invoke it or not. This is entirely appropriate. If the court is to have the power to redistribute property rights via the powerful

³¹ [1989] 2 NZLR 180.

³² [1993] 1 NZLR 257.

³³ [1994] NZLR 385.

³⁴ At 405 and 401.

weapon of the remedial constructive trust, the potential “victims” must have some indication of the circumstances that will render their property rights vulnerable. As Henry J pointed out, there has been insufficient development in the last decade.

2. *The underlying principles in previous cases*

In *Elders Pastoral Ltd*,³⁵ the underlying principle was unconscionability.³⁶ In *Liggett v Kensington*,³⁷ Gault J, while unwilling “to attempt any general judicial formulation” of the underlying principles, granted relief on the basis of the insolvent company’s overall “inequitable and unconscionable conduct”, subject to consideration of the competing claim of the secured creditor. He indicated that he would be reluctant to impose a constructive trust if the secured creditor had obtained its security for value and without notice of the circumstances underlying the plaintiffs’ claim. The latter factors seemed to go to remedial discretion rather than to the initial availability of remedy question, but were irrelevant as His Honour considered that the secured creditor had notice.

McKay J, discussing the *Elders* “unconscionability” test, noted that

this does not mean that a constructive trust is to be imposed on the basis of some vague idea of what might seem fair. It is used...to prevent a person from retaining a benefit in breach of his legal or equitable obligations.³⁸

Although the basis of the non-allocated claimants’ claim in the Privy Council in *Re Goldcorp Exchange Ltd*³⁹ does not emerge clearly from the advice, it appears to have been advanced on the grounds of unjust enrichment, injurious dealing with the subject matter of the alleged trust, or some wider equitable principle (perhaps unconscionability). While noting that the doctrine underpinning the remedy “is still in an early stage and no single juristic account of it has yet been agreed”, Lord Mustill firmly

³⁵ [1989] 2 NZLR 180.

³⁶ See generally Rotheram, “The Redistributive Constructive Trust: Confounding Ownership with Obligation” (1992) 5 *Canterbury Law Review* 84, and Dixon, “The Remedial Constructive Trust Based on Unconscionability in the New Zealand Environment” (1992) 7 *AULR* 147.

³⁷ [1993] 1 NZLR 257, 281 and 282.

³⁸ At 293. Cooke J, the third member of the court (who had also sat in *Elders*) did not need to consider the availability of a redistributive remedy in this case as he found for the claimants on other grounds.

³⁹ [1994] 3 NZLR 385, 400.

rejected any approach based on a new equity permitting intervention to redress an imbalance between the two parties.⁴⁰

3. Unconscionability as a single foundational principle in Fortex for both institutional and remedial constructive trusts

Whereas Gallen J's judgment in the High Court sought the underlying principles from within the law of restitution, the Court of Appeal's joint judgment showed more than the consistent reluctance to apply unjust enrichment doctrine and preference for the application of equitable principles noted by New Zealand commentators in the early 1990's.⁴¹ Here unconscionability was the clear victor.

The remedial constructive trust seems to have been regarded as operating within the law of property as the means by which equity restrains the unconscionable exercise of legal property rights. It was not seen as having any competence within the law of restitution (itself part of the law of obligations) because conscience "is the *whole* basis upon which equity intervenes to restrain reliance on rights at law".⁴² As the unjust enrichment principle operates on a strict liability basis subject to the availability of certain defences, this is a clear indication that unconscionability is now the *sole* foundational principle in New Zealand for the imposition of a remedial constructive trust over property to which others have legal rights.

The decision also clarifies the concept of unconscionability. Where, on insolvency, the original defendant has effectively been eliminated from the picture and the secured creditors have rights to the assets, it is their conscience which is crucial. As this factor led to the conclusion that the remedial constructive trust was not available as a matter of principle, it was not necessary to consider whether it should be granted as a matter of discretion, and the decision contains no indication of what factors might be relevant to that inquiry.

4. The subject matter or identifiability issue for remedial constructive trusts

Although identifiable subject matter is not required in this context, neither initially nor for tracing purposes, Thorp J, in the High Court in the opening

⁴⁰ At 404.

⁴¹ Peart, "A Comparative View of Property Rights in De Facto Relationships: Are we all driving in the same direction?" (1989) 7 OLR 100, 133, and Dixon, *supra* note 36, at 164.

⁴² [1998] 3 NZLR 171, 177 (emphasis added).

stage of the *Goldcorp* litigation,⁴³ required a causal connection between the unconscionable conduct and the alleged subject matter. On appeal, McKay J saw the existence of a causal nexus between the claimant and the property in respect of which a constructive trust is sought as a relevant consideration without deciding whether it was essential. In the Privy Council, Lord Mustill noted, in denying the claim, that “the Company’s stock of bullion had no connection with the claimants’ purchases, and to enable the claimants to reach out and ... abstract it ..would give them an adventitious benefit”.⁴⁴

Unfortunately this issue was disposed of very briefly in the joint judgment in *Fortex* without any indication of when the Court might find it “appropriate” to impose a trust on assets in the defendant’s hands.⁴⁵

5. The subject matter or identifiability issue for express and institutional constructive trusts

This issue was at the heart of the *Goldcorp* decision. There never had been any identifiable bullion to which any trust could attach. Without identifiable subject matter there could be no express or institutional constructive trust. The judgment in *Fortex* makes the point that where the subject matter of the alleged trust is money there must be a separately identifiable *fund*. A credit balance would therefore be insufficient without specific appropriation.

V. CONCLUSIONS

Although the remedial constructive trust has been available in the commercial sphere for nearly a decade, its juristic basis has been opened and therefore productive of much uncertainty. While this will often be the case with new developments, the Court of Appeal, in a decision which will be welcomed by the commercial community, has clearly indicated the need for future articulation of the underlying doctrine and its requirements with greater precision. This is commendable.

The Court also gave a strong indication that unconscionability rather than unjust enrichment was the single underlying principle. Although this has the attraction of simplicity it is not clear why unjust enrichment should be ruled out. Certainty does not require its rejection and indeed may be better served

⁴³ *Robinson v Goldcorp Refiners Limited (In Receivership)*, unreported, High Court, Auckland, 17 October 1990, Thorp J.

⁴⁴ [1994] NZLR 385, 400-401.

⁴⁵ For a discussion of causal link, see Fardell, and Fulton, *supra* note 18.

by a meticulous analysis of the facts within the framework of unjust enrichment.⁴⁶

These matters await resolution for another day. *Fortex* provides notice that the Court of Appeal is minded to take a very close look at the remedial constructive trust when that day dawns.

⁴⁶ Cf Lord Browne-Wilkinson's recent suggestion in *Westdeutsche Landesbank Girozentrale v Islington Borough Council* [1996] 2 All ER 961, 999 that proprietary restitutionary remedies might be developed by the recognition of the remedial constructive trust in English law: "The court by way of remedy might impose a constructive trust on a defendant who knowingly retains property of which the plaintiff has been unjustly deprived. Since the remedy can be tailored to the circumstances of the case, innocent third parties would not be prejudiced and restitutionary defences such as change of position, are capable of being given effect". See also the discussion of the above suggestion in Friar, "Equity, Restitution and Commercial Commonsense" [1996] NZLJ 447, 449 and 450.

BOOK REVIEWS

THE TREATY MAKING PROCESS: REFORM AND THE ROLE OF PARLIAMENT, Law Commission, Report 45. Wellington, 1997, ix and 138 pp.

This Report is part of the Law Commission's International Obligations Project which aims to improve the awareness of international law in New Zealand, including New Zealand's international rights and obligations and the means by which these are created. It follows on from the earlier Commission Report, *A New Zealand Guide to International Law and its Sources* (NZLC R34 1996). The Report describes the then current treaty making process, with an emphasis on the role of Parliament. It also contains two interesting Appendices on overseas practice and experience of treaty making and implementation, internet websites relevant to treaties, and treaty making. As a resource for those working in the area, these Appendices are invaluable.

The argument of the Report focuses on the need for a greater involvement by Parliament in the whole process of treaty making. The rationale for the argument rests on the increasing reality of globalisation for individual citizens as well as organisations and governments. This reality is expressed in the growing number of multilateral and bilateral treaties to which New Zealand is a partner. The relevance of these treaties to the actions of New Zealanders has in the past depended largely on whether the obligations under the treaties have been incorporated into domestic legislation. There has been a recent trend, not only in New Zealand courts but also in other common law jurisdictions, for the courts to give more weight to international obligations. After reference to the cases of *Tavita v Minister of Immigration* [1994] 2 NZLR 257 and *New Zealand Airline Pilots' Association Inc v Attorney-General*, unreported, 16 June 1997, CA 300/96, the Report concludes with the observation that "[i]n summary, when considering the treaty making process, it should not be thought that a treaty which has not been the subject of legislation is irrelevant to the New Zealand legal system".

However, the Report is more concerned with the way in which treaties are made and implemented than in their interpretation. The recommendations of the Report reflect this emphasis. It is worth recording these recommendations because events subsequent to the Report have resulted in their substantive implementation by government, changing the procedure for treaty making. The recommendations were: -

RECOMMENDATION 1 - That the value of notification and consultation with Parliament and interested or affected groups at the negotiating stage of the treaty making process be recognised, with the purpose of developing and formalising such practices.

RECOMMENDATION 1A - That consideration be given to the establishment of a Treaty Committee of Parliament.

RECOMMENDATION 2 - That consideration be given to the introduction of a practice of the timely tabling of treaties so that the members of the House of Representatives can determine whether they wish to consider the government's proposed action.

RECOMMENDATION 2A - That consideration be given to the preparation of a treaty impact statement for all treaties to which New Zealand proposes to become a party.

RECOMMENDATION 3 - That, so far as practicable, legislation implementing treaties or other international instruments give direct effect to the texts (that is, use the original wording of the treaties), and that when that is not possible, the legislation indicate in some convenient way its treaty or other international origins.

The whole matter of the role of Parliament in treaty making was considered in the *Report of the Standing Orders Committee on its Review of the Operation of the Standing Orders* (I.18B), and in 1997 by an Inquiry held by the Foreign Affairs Defence and Trade Committee on Parliament's role in the international treaty process. The result of that inquiry was a Cabinet Office Circular CO (98) 4, 6 July 1998, setting out the requirements that must be followed before a government may ratify, accede to, accept, or approve a treaty. Treaties are defined as "international agreements concluded between states in written form, which are intended to create binding obligations at international law". The new procedure was also to apply for a trial period of the balance of the current Parliamentary term.

The Cabinet circular states that "...all treaties which require the formal steps of ratification, accession, acceptance, or approval and have been considered by Cabinet, must be presented to the House before these formal steps can proceed". The treaty is referred to the Foreign Affairs Defence and Trade Committee of the House, which may inquire into it or refer it to a more appropriate committee. The government will not take any binding action on the treaty until the relevant committee has reported or 35 days (or 45 days if tabled after 15 December) have elapsed from the date of tabling, whichever is sooner. Treaties presented to the House must be accompanied by a

National Interest Analysis. The Analysis must include matters relating to the reasons for New Zealand becoming a party to the treaty; the obligation imposed on New Zealand and any reservations; the cost involved; future protocols; implementation measures, including legislation required; the consultation that have been undertaken or are proposed; and if there is any withdrawal or denunciation clause. Thus, while the Commission's recommendations have not been totally implemented, their substance has been incorporated into the treaty making process.

The importance of treaties and the need for greater community and parliamentary involvement was addressed at a recent conference of the International Law Association on "Treaties and New Zealand Law". The proceedings of this conference, which included several interesting addresses from Australian academics and practitioners, would be essential reading for anyone interested in this area. For the academic, the lesson that emerged from the conference and the reading of the Commission's Report is that international law must now be mainstreamed into all our teaching programs. It is no longer the optional course provided for the few who may wish to enter the world of diplomacy. A knowledge of treaties is now essential for all practitioners, whose clients in all their myriad of activities will find themselves requiring knowledge of their international obligations.

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PRINCIPLES OF CRIMINAL LAW, by AP Simester and WJ Brookbanks. Wellington, Brooker's, 1998, lv and 686pp, including index. Price \$99 including GST (softcover).

ADAMS ON CRIMINAL LAW 2ND STUDENT EDITION, by J Bruce Robertson (ed). Wellington, Brooker's, 1998, xcvi and 1034 pp, including index. Price \$69.75 (softcover).

In New Zealand criminal law was long taught without the benefit of an indigenous textbook. Improvement began in 1996, with the first student edition of *Adams on Criminal Law*. With the simultaneous publication this year of Simester and Brookbanks' *Principles of Law* ("*Principles*") and a second student edition of *Adams on Criminal Law* ("*Adams*"), there is almost an embarrassment of riches for those seeking an introductory treatment of New Zealand criminal law. These two books have the same publisher and two of the three authors of *Principles* also contribute to *Adams*. However, there are fundamental differences between the two works.

To start with, the goals of *Adams* and *Principles* are not the same. The parent volume of *Adams* takes up three looseleaf volumes, described in the preface to the student edition as "an invaluable reference book for Judges, academics, and practitioners". The student edition takes material from three chapters of the looseleaf volumes but has the same format. It is basically a heavily annotated Crimes Act 1961, although there are also sections dealing with the law of evidence and the application of the New Zealand Bill of Rights Act 1990. The work is a superb source of case references: the case table runs to over 50 pages of small print. The bulk of it is devoted to the requirements of specific offences because the Crimes Act is primarily concerned with these.

By contrast, the goal of *Principles* is to "explain the general doctrines of criminal responsibility and the specific law of the core substantive offences...in a manner that both states the law and identifies the issues of principle and policy which gird and shape that law" (p vii). The organisation does not follow the order of the Crimes Act itself: it mirrors the structure of an introduction to criminal law. It starts with general principles, continues with derivative liability and inchoate offences, and spends seven chapters on defences, before reaching some selected specific offences. Parts of the Crimes Act are omitted altogether. Questions of evidence rarely intrude into a criminal law course, and *Principles* does not include chapters on evidence or Bill of Rights issues.

The different goals lead to differences of style and explanatory technique. *Adams* and *Principles* both refer to the rule that a person might have a good

motive and still possess the *mens rea* for an offence. *Adams* states the rule and supports it with a list of five cases but does not discuss the facts of any of the cases (CA 20.10(1)). *Principles* illustrates the rule with the facts of *R v Smith* [1960] 2 QB 423, in which the defendant offered a bribe to a town mayor in order to expose corruption but was still convicted of offering a bribe to a public official (p 80). Then, in a footnote, a conflicting case and some supporting cases are noted, and the comment made that the principle “which disconnects a finding of *mens rea* from the presence of fault, is appropriate only if a suitable range of defences is available” (p 80 n3). The treatment in *Principles* is fuller and it relates the rule itself to principles of responsibility. For a person who is looking for references to support an argument about motive and *mens rea*, *Adams* might be more useful. For a person who knows nothing about *mens rea*, *Principles* will provide the knowledge needed to make the most of *Adams* and to read the cases cited therein more critically.

This is not to say that one book is “better” than the other. Each has strengths and weaknesses. It is unfair to criticise *Adams* for not being a textbook or to criticise *Principles* for not being a comprehensive guide to the Crimes Act. They should be assessed according to whether they meet the goals they have set themselves.

Principles was written by several authors. Their style is not identical. For example, some but not all chapters make use of the first person. These are not serious problems and matters such as footnote style and headings are consistent. The book does not look “cobbled together”. However, there is at least one inconsistency arising from an apparent difference of opinion between the authors. In chapter 3, the discussion of negligence includes the comment that “[i]f the defendant has additional knowledge, over and above that which a reasonable man would possess, then she will be held to the standard of that extra knowledge” (p 107). The author of chapter 14 disagrees: “a higher standard does not apply merely because D has special skill or qualifications” (p 489). It may be that one chapter states what the law is and the other what the law ought to be, but the two statements do appear to be contradictory. It would have been useful to indicate that both approaches are supportable, rather than to leave readers with the impression that one author is “wrong”.

The goal of integrating theory and black-letter law is a difficult one. It involves stating the law accurately *and* explaining the principles that underlie the law *and* expressing opinions about the validity of the law built upon those principles. *Principles* does not try to do all this simultaneously. Different chapters lean towards one or other of the overall goals. The way in

which criminal law is taught is that teachers start by explaining abstract concepts like “intention” and “recklessness”, and only later apply them to actual offences. To teach in any other way would result in needless repetition. This textbook adopts a similar structure, and it is a practical one. Nonetheless, there are some things that could be done better. The theory chapters use case law to illustrate principles. To avoid confusion between description of the law and analysis of the law, a statement that this is how the case law is being used would be helpful. These are quibbles, however: *Principles* manages to combine a sophisticated discussion of principles of criminal law with a readable analysis of major offences and defences.

Adams does not purport to be a textbook, and a denser approach is appropriate to its purpose. It includes a surprisingly large amount of commentary on basic principles and many articles are noted as well as case-law. One criticism that might be made is that it is unclear which sections of the commentary have been updated for the second edition and the date to which the commentary has been updated. The inclusion of material on evidence and the New Zealand Bill of Rights Act 1990 is highly desirable, indeed necessary, if the book is to be useful for practitioners. However, doubts might be expressed about the value of this material for a student. The way in which university law courses are organised means that students rarely study criminal law and evidence in tandem. If new editions of *Adams* are to be published fairly frequently, as this second edition suggests, a student who purchases the book intending to use it for both courses might well find that it has been superseded before she starts the second course. This will either result in extra expense for a new edition of *Adams* or some other textbook, or, more alarmingly, the student may attempt to work from the out-of-date edition. The black-letter law basis of *Adams* makes this a dangerous practice. *Principles*, on the other hand, is a book into which she might continue to dip, when puzzled, for many years to come, since it does not try to provide complete coverage.

In conclusion, the answer to the question “which book should I buy?” is that, in an ideal world, students would own both, and they should certainly have access to both. *Principles* is introductory in nature although there is much in it of interest to the more advanced student. The emphasis is on teaching concepts and principles that can then be used to help the reader understand material outside the scope of his or her basic criminal law course. *Adams* is a reference tool. If it were the only book available, its sheer size would be a disadvantage. From a student's point of view, and especially if the student has no textbook to assist her, clear explanation is more important than compendious coverage. The usefulness of *Adams* is enhanced

by the availability of *Principles*: they fulfil different functions and each complements the other.

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McCaw Lewis Chapman

L A W Y E R S

THE McCAW LEWIS CHAPMAN ADVOCACY CONTEST

IN THE COURT OF APPEAL DECISION IN *R v HINES*, SHOULD A WITNESS ANONYMITY RULE HAVE BEEN DEVELOPED WHICH DEPARTED FROM THE DECISION IN *R v HUGHES*?

BY CHRISTOPHER FLATT*

SUMMARY OF SUBMISSIONS OF COUNSEL FOR THE CROWN¹

May it please your Honours, the submissions for the Crown are as follows:

1. Section 344C of the Crimes Act 1961 and section 16 of the Oaths and Declarations Act 1957 provide this Court with the discretion to allow anonymity to Witness A.
2. There is a substantive body of domestic and international law that supports the availability of witness anonymity once the court has established the credibility of the witness.
3. The development of witness anonymity rules are legal developments within the law of evidence and procedure and therefore providing anonymity for Witness A will not encroach upon the constitutional authority of Parliament.

SUBMISSION ONE

Section 344C of the Crimes Act 1961 and section 16 of the Oaths and Declarations Act 1957 provide this Court with the discretion to allow anonymity to Witness A.

Section 344C(3) of the Crimes Act 1961 allows a judge to make an order excusing the disclosure of an identification witness's name and address to the defendant if the judge is satisfied that such an order "is necessary to protect the identification witness or any other person". Detective Senior Sergeant Lyons, the police officer who undertook the inquiries into Witness A's background and credibility, has openly admitted that the police will not be able to provide Witness A with adequate protection in the future. There is a growing trend by gang members to use violence to intimidate potential

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¹ For the purposes of this contest, students were asked to imagine they were re-arguing for either counsel within the Court of Appeal case of *R v Hines* [1997] 3 NZLR 529. As such the amendments introduced by the Evidence (Witness Anonymity) Amendment Act 1997 did not apply for the purposes of this contest.

witnesses to prevent them from testifying in court. I refer to *R v Coleman*² and *M v Attorney-General*.³ As a result of these cases and other publicly reported attacks, Witness A is understandably extremely afraid of retaliation if he does not receive witness anonymity when he delivers his evidence.

Anonymity under section 344C(3) is confined to identification witnesses, defined in section 344C(1) as a person who claims to have seen the offender in the circumstances of the offence. In this case, whilst peering through the slats of the portable toilet he was occupying, Witness A had a clear view of the stabbing and Mr Hines' participation in it. Thus it is clear, as supported by Ellis J's decision to grant a consent order excusing disclosure of his name prior to trial, that Witness A satisfied the requirements of section 344C(3). Section 344C(3) does not explicitly state when such an order cuts out. Section 344C(2) indicates that it relates to "any time after a person has been charged with an offence". Therefore the provisions of the statute do not expressly prevent Witness A's anonymity, under section 344C(3), from extending into the trial of Mr Hines.

This anonymity is further supported by the "Scots Form" oath as contained within section 16 of the Oaths and Declarations Act 1957. This section entitles every witness in any civil or criminal proceeding, if he or she so wishes, to take this oath instead of the oath usually administered to witnesses. The words of this oath are "I swear by Almighty God, as I shall answer to God at the great day of judgment, that I will speak the truth, the whole truth, and nothing but the truth". Therefore section 16 allows Witness A to be officially sworn into court while still retaining his anonymity as provided for in section 344C of the Crimes Act 1961.

It is therefore submitted that the statutory authority as contained within both section 344C(3) of the Crimes Act 1961 and section 16 of the Oaths and Declarations Act 1957 do provide this Court with the discretion to allow anonymity to Witness A. Submission Two will now examine why this discretion should be extended to the present case.

SUBMISSION TWO

There is a substantive body of domestic and international common law that supports the availability of witness anonymity once the court has established the credibility of the witness.

² (1996) 14 CRNZ 258.

³ Unreported, Court of Appeal, Wellington, CA 60/97, 29 May 1997.

*R v Hughes*⁴ centred upon, but was not confined to, the anonymity of undercover police officers as witnesses. The right to confront an adverse witness was held to be basic to any civilised notion of a fair trial and therefore the Court of Appeal by a majority of three to two held that undercover police officers did have to reveal their true name and address when giving evidence. In response to this decision, Parliament rapidly introduced the Evidence Amendment Act 1986 which in essence overturned the *R v Hughes* decision by legislating for the anonymity of undercover police officers in cases involving specified crimes.

In *Collector of Customs v Lawrence Publishing Co Ltd*,⁵ it was held that the Court of Appeal will ordinarily follow its earlier decisions but will be prepared to review and affirm, modify or overrule an earlier decision where it is satisfied that it should do so. It is submitted that *R v Hughes* is clearly a decision which should be modified or overruled, in so far as it still applies to witnesses other than undercover police officers.

Over the last decade there has been a gradual yet substantial movement away from the *R v Hughes* decision within the New Zealand common law relating to the availability of witness anonymity. In *R v L*,⁶ the Court of Appeal held that a sworn statement of an alleged rape victim who had died after depositions, but before trial, could be proved in evidence even though the accused had taken no steps to seek or exercise a right of cross-examination at the depositions hearing. In *R v L*, Richardson J stated that the absence of an opportunity to cross-examine at the preliminary hearing would not affect the fairness of the ensuing trial.⁷ It is submitted that, if the Court of Appeal declares that the absence of an opportunity to cross-examine a witness does not pose a threat to the fairness of a trial, clearly the anonymity of Witness A, a witness who has had his credibility endorsed by the police, can in no possible way pose a threat to the fairness of Mr Hines' trial.

In *R v Coleman*,⁸ Baragwanath J held that where the evidence is critical to whether the trial can take place and the court is satisfied that there is no substantial reason, following due inquiry, to doubt the credibility of a witness, then the court has the jurisdiction to permit anonymous evidence. As mentioned earlier, Detective Senior Sergeant Lyons has made substantial

⁴ [1986] 2 NZLR 129.

⁵ [1986] 1 NZLR 404, 414.

⁶ [1994] 2 NZLR 54.

⁷ At 63.

⁸ (1996) 14 CRNZ 258.

inquiries into the credibility of Witness A, as the police knew nothing about him before he came forward.

It has been ascertained that, apart from a drunk-driving conviction some 20 years ago, Witness A does not have a criminal record, he is not affiliated with any organisation, and he has sought no material benefit or gain from the police. Detective Senior Sergeant Lyons has stated that he is satisfied that Witness A is a genuine and honest citizen. The police have also stated that Witness A's evidence is crucial to a successful conviction of Mr Hines. It therefore follows that, as a result of the decision in *R v Coleman*, this Court has the authority to extend witness anonymity to Witness A.

There has also been substantial development in the English common law relating to the availability of witness anonymity. In *R v Watford Magistrates' Court, ex parte Lenman*,⁹ a witness who was reluctant to testify due to fear of retaliation was permitted to give evidence anonymously. In *R v Taylor*,¹⁰ the English Court of Appeal held that witness anonymity can be allowed at the discretion of the trial judge.

The Court in *R v Taylor* held there are certain relevant factors that must exist before judicial discretion can be exercised: that there are real grounds for being fearful of the consequences of giving non-anonymous evidence; that the evidence is sufficiently relevant and important to the prosecution's case; that the court is satisfied as to the creditworthiness of the witness; and that the court is satisfied that no undue prejudice is caused to the defendant. As mentioned in the above submissions, Witness A and this trial satisfy these criteria. In *R v Liverpool City Magistrates' Court, ex parte Director of Public Prosecutions*,¹¹ Beldam LJ and Smith J adopted a similar approach and endorsed the criteria of relevant factors contained in *R v Taylor*.

It is submitted that over the last decade the common law in both New Zealand and England has progressed down a different path from that of *R v Hughes*. Current precedent establishes that, once the credibility of a witness, the necessity of their evidence, and the absence of any injustice for the accused have been proven, courts are entitled to protect the anonymity of witnesses. It is submitted that the current case fulfils all these requirements and this Court is bound to protect the anonymity of Witness A by dismissing the appeal.

⁹ [1993] Crim LR 388 (Queen's Bench Divisional Court).

¹⁰ [1994] Times LR 484; [1995] Crim LR 253.

¹¹ Queen's Bench Division, CO 1148/96, 19 July 1996.

SUBMISSION THREE

The development of witness anonymity rules are legal developments within the law of evidence and procedure and, as such, providing anonymity for Witness A will not encroach upon the constitutional authority of Parliament.

R v Hughes contains clear statements of two conflicting views: one that the accused's rights should be limited only by the legislature; the other that the evidence to be given and the manner in which it is given are matters singularly appropriate for determination by the courts, drawing upon trial experience and employing the flexibility of case-by-case consideration. In *Myers v Director of Public Prosecutions*,¹² Lord Reid stated that, if the courts are to extend the law, it must be for the development and application of fundamental principles; the court cannot introduce arbitrary conditions or limitations, which must be left to Parliament. Viscount Simmonds, in *Shaw v Director of Public Prosecutions*,¹³ stated that in the area of criminal law there remains in the courts of law a residual power to enforce the supreme and fundamental purpose of the law, to conserve not only the safety and order but also the moral welfare of the State.

Allowing witness anonymity for Witness A will not result in the introduction of a new condition or limitation to the law, or even fashion a totally new common law rule. As submission two identifies, in both New Zealand and English jurisprudence, witness anonymity is a recognised principle which has been repeatedly applied over the last decade. As McMullin J stated in *R v Hughes*, the law of evidence is largely the development of case law which the courts, not Parliament, have had to evolve in many areas to balance competing interests.¹⁴ In the same case, Cooke P stated that the question of witness anonymity falls within the fields of evidence and the inherent jurisdiction of courts, both of them fields in which the law is basically judge-made.¹⁵

Simply because the issue of witness anonymity is currently the focus of a Law Commission inquiry should not deter this Court from applying the law in the case of Witness A, for it is with Witness A and Mr Hines that this case is ultimately concerned. Though the Law Commission has expressed itself in favour of an anonymity rule, there is no assurance that any recommendations that might be made will find their way into the legislative

¹² [1965] AC 1001, 1021-1022.

¹³ [1962] AC 220, 267.

¹⁴ At 153.

¹⁵ At 135.

programme. If there is injustice capable of being alleviated, even in the short term, this Court should not abdicate responsibility for addressing it.

It would be a travesty of justice for this Court to refuse to follow the current developments in the law relating to witness anonymity, merely because a Law Commission discussion paper is currently being circulated. It is submitted that Witness A should be allowed anonymity as the issue is clearly one relating to the law of criminal evidence and procedure, and will not encroach upon the constitutional authority of Parliament. This appeal should be dismissed.

In summary the submissions for the Crown are as follows:

1. That this Court is provided the discretion to allow witness anonymity to Witness A by both section 344C of the Crimes Act 1961 and section 16 of the Oaths and Declarations Act 1957.
2. Having established the credibility of Witness A, there is a substantive body of both domestic and international common law that supports the availability of witness anonymity for Witness A.
3. Providing witness anonymity for Witness A will not encroach upon the constitutional authority of Parliament as the development of witness anonymity rules are legal developments within the law of evidence and procedure.