

**IN THE COURT OF APPEAL OF NEW ZEALAND**

**CA108/05**

BETWEEN                      AMP GENERAL INSURANCE LIMITED  
Appellant

AND                              MACALISTER TODD PHILLIPS  
BODKINS  
First Respondent

AND                              GRAEME MORRIS TODD  
Second Respondent

Hearing:                      21 November 2005

Court:                              Robertson, Baragwanath and Doogue JJ

Counsel:                      N A Till for Appellant  
E D Wylie QC for Respondents

Judgment:                      15 December 2005

---

**JUDGMENT OF THE COURT**

---

- A      The amount for which judgment is entered in favour of the respondents is reduced from \$70,000 to \$50,486.10.**
- B      The interest to which the respondents are entitled is reduced proportionately.**
- C      In all other respects the appeal is dismissed.**
- D      There is no order as to costs.**
-

## REASONS

(Given by Baragwanath J)

[1] The second respondent, Mr Todd, and the first respondent, the law firm of which he is a partner, succeeded in a claim in the High Court against their professional indemnifier (AMP). Chisholm J held that a sum of \$72,000 paid by the firm to settle a tax debt to the Commissioner of Inland Revenue, together with interest and the costs incurred by the firm in negotiating settlement, were recoverable under their policy of insurance. AMP appeals against the decision and submits that the judgment in favour of the respondents should be set aside.

### Background facts

[2] Since the 1980s the firm has acted for Mr Basil Walker, his wife and members of their immediate family. Mr Todd, on behalf of the firm, acted on the creation of the Walker Family Trust of which Mr Basil Walker was the effective settlor. Under a deed dated 20 April 1993 his brother Lindsay and Mr Todd were appointed trustees. Mr Basil Walker, his wife and family were named as primary beneficiaries. As well as accepting his role as trustee, Mr Todd assumed primary responsibility for advising and acting for the Trust as its solicitor; other partners and staff also provided professional services from time to time.

[3] In April 1994 the trustees bought a property at Towne Place, Queenstown, intending to construct seven residential units to be registered under the Unit Titles Act 1972. Substantial mortgage finance was provided by the Bank of New Zealand. The mortgage document was not produced at trial and its terms were not proved.

[4] The trustees agreed that Mr Basil Walker should carry out the development of the Towne Place units on behalf of the trust. He undertook to attend to the necessary GST and other tax responsibilities as well as to the accounting in relation to the development. Counsel were unable to refer us to any authority permitting the trustees to delegate those functions in this way: cf Dal Pont and Chambers *Equity and Trusts in Australia and New Zealand* (2<sup>nd</sup> ed) at 625:

The duty not to delegate the exercise of a trustee's powers, authorities and discretions arising under the trust, either to the co-trustee or a third party, is a corollary of the duty to act personally (*McMillan v McMillan* (1891) 17 VLR 33, 38-9).

The function of accounting for GST remained the trustees' responsibility.

[5] The trustees subsequently bought further land at Lake Hayes and at Frankton Road, Queenstown. The trustees had expected to be able to use the proceeds of sale of the Towne Place units to complete the latter purchase but because of delays they found it necessary to arrange further BNZ funding to settle the Frankton Road purchase.

[6] The sales of the Towne Place units were progressively settled from March to May 1995. To facilitate the settlements BNZ by letter of 23 March 1995 wrote to the firm stating:

...we enclose memorandum of mortgage 864045/2 as requested against your undertaking to provide the Bank with the balance sale proceeds of each unit on completion of settlement.

We will return to the question whether "the balance sale proceeds" was to include or exclude GST.

[7] During the process of settlement of the sales Mr Todd and his legal executive, acting as solicitors for the trustees, overlooked that GST was payable by the trustees on each sale. The whole of the net proceeds was paid to BNZ in reduction of its mortgage without any provision for the payment to the Commissioner of GST.

[8] Later developments relating to the Trust do not need to be detailed. It is common ground that the trustees were personally liable to the Commissioner for that GST debt: Goods and Services Tax Act 1985 s 57(3). As at 30 April 1995 the GST liability incurred on the sale of the Towne Place units was \$50,486.10. As at 15 March 2001 the total amount of GST, other taxes, penalties and interest amounted to \$278,330.

[9] In September 2001 Mr Lindsay Walker issued a proceeding against Mr Todd alleging breach of his duty as solicitor and trustee and seeking a declaration that he was entitled to indemnity from Mr Todd in relation to any tax liability. AMP took over the defence of the proceeding and issued a counter-claim against Mr Lindsay Walker seeking half the amount of \$72,000 that it was expected Mr Todd would have to pay to the Commissioner to settle the tax claim against him. In a separate proceeding Mr Todd sued the Trust's accountants for professional negligence.

[10] During 2002 settlement of these claims was achieved among various parties. The Commissioner accepted \$72,000 from Mr Todd and \$30,000 from Mr Lindsay Walker in satisfaction of their personal liability as trustees, the firm borrowing money in order to meet Mr Todd's liability. The claim by Mr Todd against the Trust's accountants was settled by their paying \$20,000. Mr Lindsay Walker's claim against Mr Todd was settled by payment of \$27,000 plus a share of a mediator's fee. The firm contributed \$20,000, being the excess under the policy, and AMP contributed the balance required to complete this part of the settlement.

[11] The present proceeding by the firm and Mr Todd, claiming indemnity against AMP under their insurance policy, was issued on 4 November 2003.

### **The policy**

[12] The policy provided:

#### **OPERATIVE CLAUSE**

*AMP agrees, subject to the terms, limitations, exclusions and conditions of this Policy to indemnify the Insured in respect of claims first made against, or losses first discovered by the Insured after the inception of this Policy arising out of the conduct of the Professional Services of the Insured for*

1. *claims (including claimants' costs) made against the Insured arising out of civil liability, and losses incurred by the Insured due to dishonesty of employees.*
2. *other costs and expenses incurred by the Insured in the defence and/or settlement of claims or losses under Operative Clause 1.*

... (emphasis added)

The policy does not define the words “*claims*”, “*losses*” and “*civil liability*”.

[13] “*Professional Services*” carries the following definition:

advice or services performed in the conduct of the profession, which shall also include when acting as trustees, stated in the Schedule by or on behalf of the Insured or duties undertaken by the Firm or Practice as agents of other practitioners excluding any individual personal appointments of a present partner, outgoing partner, sole practitioner or employee of the Firm or Practice as a Director or Officer unless liability arises from the professional advice given in the capacity of the profession as stated in the Schedule.

The profession stated in the schedule is that of solicitors.

[14] Exclusion 8 provides:

AMP shall not indemnify the insured against a claim or loss... arising from their trading loss or trading liability incurred by a business managed by or carried on by the Insured.

### **The judgment of the High Court**

[15] The Judge gave the following reasons for his decision in favour of the respondents:

[42] In his capacity as a solicitor Mr Todd failed to exercise proper care and skill when acting on the sale of the units. Failure to make provision for GST speaks for itself. Mr Todd accepts that he was negligent. Expert evidence from Mr Mackintosh supports that conclusion and no serious argument to the contrary was advanced on behalf of the defendant. The firm was, of course, responsible for Mr Todd’s negligence.

[43] Failure to pay GST from the sale proceeds of each Towne Place unit carried the direct, although not immediate, consequences that the tax could not be met from the assets of the trust and the trustees became personally liable for the tax and penalties under the Goods and Services Tax Act. This situation would not have arisen if the firm (through Mr Todd) had properly discharged its conveyancing responsibilities when acting on the sale of each unit.

[44] Initially the trustees were hopeful that it would be possible to retrieve the situation by selling trust assets. In fact, however, despite their best efforts the trustees were unable to retrieve the situation. The trust was insolvent. Consequently the trustees faced the prospect of meeting the GST and penalties from their own pockets. This was directly attributable to the firm’s negligence. If the firm had not borrowed the money and paid the sum of \$72,000 to IRD, Mr Todd would have been entitled to issue proceedings

and recover from the firm the amount that he was required to pay to IRD (in all probability much more than \$72,000). The firm's acknowledgement of liability and willingness to settle with IRD to avoid an escalating claim was plainly sensible. The insurer was kept informed throughout and it is difficult to imagine that the outcome would have been any different if the insurer had been handling the claim. It might also be added that if Mr Walker's claim against Mr Todd had gone the full distance it would not have been surprising if the trust's accountants had taken steps to join the firm.

[45] Mr Till maintains that there was no loss because the trust was credited with the GST and that Mr Todd's loss resulted from the absence of a solvent trust fund against which to enforce his right of indemnity. I do not accept those submissions. Mr Todd's liability to pay GST and penalties out of his own pocket was directly attributable to the firm's negligence. Without that negligence there would not have been any question of Mr Todd having to pay GST and penalties on behalf of the trust because they would have been met by the trust out of the sale proceeds of each unit.

[46] The underlying reality of the claim against the firm can now be stated. In his capacity as a trustee of the Walker Family Trust Mr Todd had a valid claim against the firm for its negligence (so did Mr Walker). This was acknowledged by the firm. AMP chose not to be directly involved in the efforts of the firm and Mr Todd to settle Mr Todd's claim as expeditiously as possible. Although the settlement with IRD (funded by the firm) avoided the necessity for Mr Todd to formally bring his claim and issue proceedings, it does not alter the reality that Mr Todd (and Mr Walker) had a valid claim against the firm which fell within the operative clause of the policy.

[47] The next issue is whether Exclusion 8 of the policy applies. This provision excludes claims or losses "arising from a trading loss or trading liability incurred by a business managed by or carried on by the Insured". The defendant maintains that the tax liabilities arose from the trust's losses and from trading managed and/or carried out by the plaintiffs. In my view that proposition distorts the actual situation. The claim in this case arose from the firm's failure to make provision for GST when acting on the sale of the Towne Place units. It did not arise from a trading loss or trading liability incurred by a business managed or carried on by the insured. The insured was carrying on business as solicitors, not as a property developer operating under the name of the Walker Family Trust.

[48] In the end result I am satisfied that the first plaintiff is entitled to indemnity under the policy in relation to the sum of \$72,000 paid by it to IRD. Given Mr Till's concession ..., it is my understanding that the conclusion I have reached (and the path by which it has been reached) means that the defendant concedes that the first plaintiff has paid the excess under the policy. Even if the defendant had not made that concession I would still have held against the defendant on the excess issue. The plaintiffs are also entitled to interest and to be reimbursed for the proportion of Mr Wylie's fee that is attributable to the settlement with the Inland Revenue Department.

## Submissions

[16] AMP submitted:

- (a) the firm and Mr Todd had no duty as solicitors to pay or make provision for payment for the GST liabilities of the trustees of the Trust;
- (b) no loss resulted to the trustees by reason of the payment of the proceeds of sale into the trustees' account with the BNZ without deduction of the GST. The trustees' GST liability arose from their inability to secure indemnity because there were insufficient trust assets;
- (c) the trustees' liability to pay GST arose from the sale of the properties and was excluded by Exclusion 8 of the policy as being a claim of loss arising from a trading loss or liability incurred by the business of the Trust managed by or carried on by the trustees.

[17] The solvency of the trust at the time of the transactions was not raised as an issue by AMP or advanced in argument before the High Court. The topic did receive some mention in oral argument in response to questions from this Court. However the litigation has been conducted throughout on the basis that the trust was solvent at the relevant time, notwithstanding that it was later found to be insolvent.

[18] Nor was there challenge by AMP to the existence of a duty owed by Mr Todd as solicitor to himself as trustee. We have therefore heard no argument on that topic.

[19] The firm and Mr Todd challenged each argument, submitting:

- (a) it was indeed their duty both to advise the trustees of the need to pay GST and to pay its amount not to the BNZ but to the Commissioner;
- (b) the trustees did sustain loss by reason of breach of such duties;

- (c) the trustees' liability to pay GST arose not from the sale of the properties but from the firm's and Mr Todd's failure to advise the trustees of the need to pay GST and the further failure to pay its amount to the Commissioner rather than to the BNZ.

## **Discussion**

### *Mr Todd's two roles*

[20] Mr Todd's role in relation to the trust was 1) as a solicitor and 2) as trustee of the Trust.

[21] Mr Todd as solicitor both failed to advise himself and his co-trustee of their duty to account for GST when the trust sold the property and to deduct from the payment to the BNZ the amount of the GST. It is therefore argued for him and the firm that the cause of the trustees' loss is that failure, so he and they are liable to the trustees in their capacity as solicitors and such liability falls within the policy and gives rise to indemnity.

[22] Certainly Mr Todd as trustee is personally liable for both the GST debt to the Commissioner and the trust's debt to the BNZ. While the policy covers certain liability as trustee its terms are circumscribed; the essential question is whether the pleaded and proved facts fall within them.

### *Trustee personally responsible for payment of GST*

[23] We have recorded ([8] above) that it is common ground that the trustees were personally liable to the Commissioner for that GST debt: Goods and Services Tax Act 1985 s 57(3).

*Trustee personally responsible for contractual liabilities of the trust...*

[24] It was observed in *CIR v Chester Trustee Services Ltd* [2003] 1 NZLR 395 at [37]:

... a trust is not a legal entity distinct from its trustee, who is personally liable to its creditors for all the debts it incurs (*Ex p Garland* (1804) 10 Ves Jun 110, *Labouchere v Tupper* (1857) 11 Moo PCC 198, *Re Graham Pitt & Bennett, ex p Nolan & Skeet* (1891) 9 NZLR 617)...

*...unless personal liability expressly excluded*

[25] Trustees can contract on terms that their personal contractual liability will not extend beyond the sum for which they can obtain indemnity from the assets of the trust. In *Re Graham Pitt & Bennett, ex p Nolan & Skeet* at 621 this Court held that:

There is no such thing recognised as that trustees have an identity different from themselves individually, and that they themselves do not become liable when acting for the trust estate, unless there is an express contract to that effect.

To similar effect are *Muir v City of Glasgow Bank* (1879) 4 App Cas 337; *Hunt Bros v Colwell* [1939] 4 All ER 406; *Helvetic Investment Corporation Pty Ltd v Knight* [1984] 9 ACLR 773 discussed in *NZHB Holdings Ltd v Bartells* (2004) 5 NZCPR 506.

*Mr Todd was aware of the option of excluding personal liability but that is not proved to have occurred*

[26] Mr Todd was aware that trustees might be able to contract out of personal liability and limit their liability to a mortgagee to the amount of the trust assets. That is apparent from his adding a clause in such terms to a letter setting out the bank's terms and conditions for a loan relating to the Frankton Road property in August 1994. But there being no evidence as to any express term to that effect in the present BNZ mortgage we must approach this case on the footing that the trustees were personally liable to the BNZ for the Towne Place borrowings.

*Are Mr Todd and the firm liable for loss triggering operation of the policy?*

[27] While Mr Todd was liable for both the BNZ and the GST debts, the claim that he and the firm are liable as solicitors (or as trustee) for a loss triggering the policy is more difficult. We have concluded that they were.

[28] To explain why certain issues need first to be cleared away.

*A payment to a creditor (the BNZ) is not treated as received in trust to the amount of any GST liability*

[29] For the reasons stated by this Court in *New Zealand Refining Co Ltd v Attorney-General* (1993) 15 NZTC 10,038, 10,052 moneys paid to a creditor in payment of a debt are not to be treated in law as in part received in trust on behalf of the Crown for payment of GST to the Crown. McKay J there contrasted the position of tax deductions made by an employer from the wages of an employee which, under s 365 of the Income Tax Act 1976, are held by the employer in trust for the Crown.

[30] In *Rob Mitchell Builder Ltd (in liquidation) v National Bank of New Zealand Ltd* (2004) 21 NZTC 18,397 Blanchard J in delivering the judgment of this Court on the point stated:

[22] ...there is nothing in the GST Act which requires a mortgagee receiving money under its mortgage in circumstances where it has not exercised a power of sale, and was not in possession of the mortgagor's land, to pay GST relating to those moneys. There are no provisions comparable to ss 5(2) and 17 under which the selling mortgagee is deemed to have made a supply in the course of a taxable activity (even if it is not registered for GST purposes), and where the transaction is segregated from other supplies and recorded in a "special return".

...

[28] The GST certainly does not have to be funded twice. The mortgagor is no worse off than it would be if the mortgagee had conducted the sale and accounted for GST. It is true that the mortgagor continues to have a debt to the Commissioner for the amount of GST in the present case. But it owes a reduced balance to its mortgagee. Its net financial position is the same as if there had been a mortgagee sale.

[31] It follows that, in the absence of authority from the BNZ, the firm had no legal right to withhold from the bank the GST payable on the sales.

*Did BNZ authorise withholding of GST?*

[32] The next question is whether the BNZ gave authority to the lawyers to deduct GST. We have reproduced the terms of the bank's authority ([6] above). It is in our view expressed too generally to be construed as an explicit authority to withhold the GST in breach of the bank's legal entitlement to receive the net proceeds of sale.

[33] The high point of the submissions of Mr Wylie QC relied on the evidence of Mr Todd. His brief which was produced in evidence in chief stated:

12. ...If I am acting for trustees, then I consider it my responsibility to tell the trustees of the GST liability and advise that if the GST is not paid, they could become personally liable for the same... Disbursements could include rates, possibly income tax, any mortgage repayment, GST commission, legal fees and any other liability triggered by the sale...

[34] His evidence in chief continued orally:

Q. We know the payment was made by the firm to BNZ. Did you intentionally pay GST to the BNZ... No, I don't believe so. There was an undertaking that had been previously given for us to pay the net proceeds of sale to the BNZ.

THE BENCH. Q. If you had turned your mind to it would GST be taken out to arrive at the net proceeds of sale or not... Yes, given that the trust was registered for GST and the bank would have been aware of that, I would have anticipated that would have been a payment which would have been accepted as part of the gross proceeds of sale before disbursement to the bank of the net proceeds of sale.

Q. Was your payment of the GST unintentional... Yes.

(reads from para 15).

Q. At that stage did you turn your mind to the possibility that you and Mr Walker were personally liable for the GST... No.

[35] Mr Wylie submitted that this evidence, on which Mr Todd was not cross-examined, establishes a preparedness on the part of the bank to accept the net proceeds of sale after deduction of GST.

[36] Read in isolation the evidence could perhaps be read as containing such an implication. But Mr Till pointed to the firm's letter of 1 November 2000 to the Commissioner writing formally on behalf of the trustees seeking relief from additional incremental tax and penalties. It contains the passage:

The debt position of the Trust was such that the money realised from sale transactions was paid to secured creditors to reduce the indebtedness. The Trustees were required to do this as a condition imposed by the first mortgagee to release their securities. The Trustees considered at all material times there would be sufficient equity upon sale of the home situated at Lake Hayes to cover the tax liability and actively pursued that option.

[37] The clear implication that the trustees were required by the bank to pay the gross amount is simply inconsistent with the contention advanced by Mr Wylie. The firm's letter was undoubtedly carefully considered and we are unable to say that the respondents have proved authority from the bank for the firm to make payment to it net of GST.

[38] It thus follows that:

- (a) at all material times the trustees are to be treated as having owed personally both the GST and the bank debt;
- (b) the Trustees had no right or duty to withhold payment to the bank of the sum required to meet their GST obligation; and
- (c) Mr Todd and his firm were, and are, liable as solicitors to the trustees because of their failure to remind the trustees that they had a GST obligation which they had to meet and for which they were entitled to reimbursement from the Trust.

*Since the Trust is to be treated as solvent the respondents have established that the claims/losses are covered by the policy*

[39] We fully accept the Judge's finding that in breach of duty Mr Todd overlooked the GST liability and gave no advice to the trustees of such liability. That could potentially have given rise to a "civil liability" for which the firm and

Mr Todd would be entitled to indemnity. To give rise to such liability, beyond nominal damages for which the respondents did not contend, the claimant must establish not only breach of duty but loss. The question whether there was a duty on Mr Todd as solicitor to pay the GST was not argued before us. We doubt that such a duty existed but leave the issue open.

[40] On the premise that the Trust was solvent, prompt and accurate advice by Mr Todd or the firm that the trustees owed the GST liability would have resulted in their seeking and obtaining payment from its assets or conceivably by recourse to further bank borrowing. That is the basis on which this case has proceeded ([17] above) and on which we must decide this appeal. It follows that the respondents have established that they committed a breach of professional duty causing actual loss which triggers AMP's liability under the policy.

#### *Summary*

[41] In summary:

- (a) Since there is no evidence as to terms of mortgage it is to be presumed that the trustees were personally liable to the bank.
- (b) They were undoubtedly personally liable to the Commissioner.
- (c) There is no evidence as to the financial position of the Trust so that the respondents have failed to discharge their onus as plaintiffs to show it was solvent.
- (d) There is no right or duty to deflect the GST moneys from the bank.
- (e) The respondents have failed to establish that the bank gave them authority to withhold the GST.
- (f) There nevertheless remained a duty on the solicitors to remind the trustees of the GST debt to the Commissioner. Their failure to do so

meant that the trustees, when called to account for the GST, could not obtain reimbursement from the Trust which was by then insolvent. The failure to provide such advice meant the firm was liable to the Trustees, including Mr Todd, and was entitled to be indemnified under the policy.

AMP did not assert that the Trust is to be treated as insolvent at the time of the payments to the BNZ. The case has proceeded on the basis that the trust was solvent at the relevant time and the appeal must be dismissed.

[42] It is common ground that to the extent, if at all, that the BNZ authorised deduction from the sums payable to it for GST it did not exceed the figure of \$50,486.10 as we have noted at [8]. Accordingly the primary judgment for the respondent is limited to that figure. The interest award must be reduced proportionately.

## **Result**

[43] The appeal is allowed and the decision of the High Court is set aside.

[44] The appeal has substantially failed but not for reasons advanced by the respondents. There will be no order as to costs in this Court.

Solicitors:

Kensington Swan, Auckland, for Appellant

Richard Butt & Associates, Christchurch, for First and Second Respondents