IN THE COURT OF APPEAL OF NEW ZEALAND

I TE KŌTI PĪRA O AOTEAROA

CA727/2017
[2019] NZCA 168

BETWEEN	PETER ANTHONY SULLIVAN First Appellant
	PORT ALBERT INVESTMENTS LIMITED Second Appellant
AND	WELLSFORD PROPERTIES LIMITED First Respondent
	GARRY EDWARD HANNAM Second Respondent

Hearing:	18 September 2018
Court:	Kós P, Winkelmann and Clifford JJ
Counsel:	P J Dale and A J Steel for Appellants J K Goodall, J P Golightly and K M Venning for Respondents
Judgment:	20 May 2019 at 11.30 am

JUDGMENT OF THE COURT

A The appeal is allowed.

B Judgment is entered for the appellants against the first and second respondents in accordance with [119] of this judgment.

C The first and second respondents must pay the appellants one set of costs for a standard appeal on a band A basis and usual disbursements.

D Costs in the High Court are to be determined in that Court.

REASONS OF THE COURT

(Given by Clifford J)

Table of Contents

Introduction

[1] In August 2014 the second appellant, Port Albert Investments Ltd — acting as nominee of the first appellant, Peter Sullivan — settled the purchase of a property (the Property) from the first respondent, Wellsford Properties Ltd.

[2] Mr Sullivan and Port Albert subsequently sued Wellsford and the second respondent Garry Hannam, a shareholder in and the sole director of Wellsford, for $428,377.43. They said that was the loss they had suffered by reason of the failure of Wellsford and Mr Hannam to disclose material information to them during their due diligence investigation of the Property.

[3] Those claims were unsuccessful in the High Court.[1] Mr Sullivan and Port Albert now appeal.

1 *Sullivan v Wellsford Properties Ltd* [2017] NZHC 3047 [High Court judgment].

Background

[4] The facts are not in material dispute. They were comprehensively recorded by Gordon J in the judgment under appeal. We can therefore summarise them reasonably succinctly for our purposes.

[5] The Property comprises a service station and an adjoining food court. There are a total of seven tenants.[2] The service station occupies the larger part of the Property. Wellsford put the Property up for sale in early June 2014. Wellsford hoped that, at a rate of return of between six and seven per cent, the Property might generate offers of close to $6 million. It engaged Jones Lang LaSalle Ltd as its agent. Jones Lang prepared and circulated an information memorandum. The information memorandum disclosed total rental income of $438,114, operating expenditure (OPEX)[3] shortfall of $32,563 and, hence, net income of $405,551. The Property came to the attention of a group of family and friends (the Group)[4] who had invested in commercial property together before. Jones Lang provided them with a copy of the information memorandum on 10 June 2014. Following discussions, the Group advised Jones Lang they were prepared to offer $5,250,000 for the Property.

[6] Jones Lang, using the standard ADLS Agreement for Sale and Purchase of Real Estate (9th edition), prepared an offer from Mr Sullivan, acting on behalf of the Group, to purchase the Property for $5,250,000. Jones Lang sent that offer to the Group on 18 June 2014.

[7] In addition to the 9th edition's standard terms, bespoke terms were included in the offer Jones Lang prepared. Those terms comprised:

(a) a due diligence clause (cl 18);

---

2 One of the tenants was in fact a licensee: that is not relevant for our purposes.

3 OPEX is an accepted abbreviation for operating expenditure. OPEX is incurred by owners of commercial properties and, subject to relevant lease terms, is typically recovered from tenants. It comprises such costs as rates, utility charges and the like.

4 Mr Sullivan acted as a disclosed agent for the Group. It was various individual members of the Group who engaged with Wellsford, Mr Hannam and Jones Lang. Rather than referring to them individually, we generally refer simply to the Group. Port Albert, as Mr Sullivan's nominee to settle the purchase, necessarily took an identical position to Mr Sullivan. We generally refer only to Mr Sullivan when discussing these proceedings against Wellsford and Mr Hannam.

(b) a confidentiality clause (cl 19);

(c) an OPEX schedule (cl 20); and

(d) a tenancy schedule as at 18 June 2014 (cl 21).

[8] As relevant, the due diligence clause provided:

> 18.0 This Agreement is conditional upon the Purchaser being satisfied that the property is suitable for the Purchaser's intended use of the property at the agreed purchase price following the Purchaser undertaking a due diligence investigation of the property, including but not limited to, an investigation of:
>
> …
>
> g) such other matters which the Purchaser ... deems pertinent including the commercial viability of the Purchaser's proposed development or use of the property.
>
> The deadline for the satisfaction of this condition is 4.00 pm on the day which is 15 working days after the date of this Agreement.
>
> This clause is inserted for the sole benefit of the Purchaser.

[9] The OPEX schedule recorded the percentages of "building" and "food court" expenses allocated to individual tenants. Those allocations both totalled 100 per cent. Those details were repeated in the tenancy schedule. Wellsford's practice was to charge each tenant a set amount for their allocated share of the OPEX each month. It would then issue a "wash-up invoice" at the end of each year to account for any variance between that amount and actual OPEX expenses.

[10] Mr Sullivan signed the offer, deleting the finance condition and adding two sub-paragraphs to the due diligence clause. Those sub-paragraphs read:

> h) The purchaser is under no obligation to supply any reasons for the purchaser's dissatisfaction with any aspect of the due diligence investigation.
>
> i) The vendor undertakes and agrees to allow the purchaser together with consultants employed by the purchaser full access to the property for the purposes of the due diligence investigation and to provide the purchaser with any information held relating to the property relevant to the due diligence investigation.

[11] Wellsford counter-offered. It increased the purchase price by $100,000 to $5,350,000 representing an implicit yield or CAP rate of 7.58 per cent.[5] Wellsford also deleted the OPEX and tenancy schedules (cls 20 and 21 respectively) and replaced them with a revised "Schedule of Tenancies". That schedule included an OPEX column.

[12] On 23 June 2014, Mr Sullivan accepted Wellsford's counter-offer, creating a binding agreement (the Agreement) between him and Wellsford for the sale and purpose of the Property, albeit subject to the satisfactory due diligence condition subsequent. That condition was to be satisfied by 14 July 2014.

[13] The Group commenced due diligence. Wellsford provided the Group and its advisers access to a data room that it had prepared. That room contained, amongst other things, copies of the various leases. OPEX became a particular focus of the Group. Notwithstanding the, albeit approximate, allocation in the Agreement's Schedule of Tenancies of 100 per cent of OPEX, it was clear from outset that not all OPEX, at least as Wellsford calculated that amount, was recovered from the tenants.

[14] In fact, the information memorandum had recorded an OPEX shortfall for the 2013 financial year of $32,563. The Group was keen to understand what generated that shortfall, and to be sure they understood its likely quantum going forward. As part of due diligence, their solicitors wrote to Wellsford's solicitors on 1 July 2014 raising a number of issues. As relevant, that letter read:

> We note that there has been a shortfall of operating expenses in the year to March 2013 and that there looks to be an effort to improve this. Please advise the reason for the shortfall and what steps have been taken to improve this position.

---

5 Commercial property can be valued on a number of different bases, including by reference to what is referred to as a CAP rate. A CAP rate is simply another phrase for the yield implied by a given value or offered purchase price on the basis of the net rental income the property will generate. The higher the yield, or CAP rate, an investor seeks in return for receipt of the assumed net income, the lower the purchase price she will be willing to pay. The creditworthiness of the tenants and the length of the remaining terms of leases will be other important considerations.

[15] The reply, again as relevant, read:

> The leases historically did not line up in terms of OPEX as methods of calculating OPEX differed in some cases. Our client has attempted to clarify and crystallise OPEX with each tenant and in recent lease documentation.

[16] The Group inquired further. Nigel Kenny, the valuer they had engaged and who had previous involvement with the Property acting for Wellsford, sought further information. Mr Kenny wanted to know the total OPEX paid by Wellsford. On 10 July 2014, Wellsford's accountants sent Mr Kenny a schedule of actual results for the year ending 31 March 2013, and forecast results for the following two years of total rent (on the basis of the rent paid by each tenant), the overall OPEX shortfall and, hence, net rent:

	F13	**Forecast F14**	**Forecast F15**
Total Rent	390,703	407,264	440,831
Net OPEX	(57,116)	52,563	(34,557)
Net Rent	333,587	354,701	406,274

[17] That information was not what Mr Kenny had wanted. In an email the next morning he told the accountants he needed to know what the actual costs were. He explained:

> In order to arrive at a realistic projection of the shortfall I need to see the actual costs incurred. Given variables in percentage recovery between rates, building expenses and food court operation this requires at least a break down by category.

[18] Later that same morning, OPEX totals for the 31 March 2014 year were provided.

[19] Later that day the Group's solicitors wrote to Wellsford's. Noting Wellsford had declined to provide its financial accounts, they inquired whether Wellsford would provide details of the last three years' rents and operating expenses, certified as correct by Wellsford's accountants. They also asked for the due diligence period to be extended to 25 July.

[20] On 14 July Wellsford's solicitors confirmed Wellsford did not want to provide its financial statements, but would provide the requested certified details as soon as possible. The due diligence period was extended as requested. That day Mr Hannam instructed Wellsford's accountants to prepare that information. The requested details were provided, via Mr Hannam, on 18 July. Total rent and total OPEX recoveries were respectively recorded as follows:

(a) For the year ending 31 March 2012: $397,815 and $176,876;

(b) For the year ending 31 March 2013: $392,912 and $177,733; and

(c) For the year ending 31 March 2014: $405,982 and $189,044.

[21] It was noted that the figures were based on invoices issued, including annual wash-up invoices; that OPEX had varied over the years "mainly due to fluctuating cleaning costs and repairs and maintenance"; and that wash-up for one tenant had not yet been done.

[22] Reflecting their interest in "the actual costs" incurred, the Group were still not satisfied. On several occasions over the following days the Group emphasised they wanted to know what the actual OPEX costs were, as opposed to what Wellsford had been invoicing. On 21 July Wellsford's solicitors asked its accountants to email "the actual OPEX our client is incurring for the property (as opposed to what it is recovering from the tenants)". Wellsford's accountants provided that information the same day. Actual OPEX incurred by Wellsford was disclosed as being $231,540, $234,096 and $259,501 (GST exclusive) for the years ending 31 March 2012, 2013 and 2014 respectively. Given Wellsford had disclosed OPEX invoices totalling $189,044 for the year to 31 March 2014, there was a disclosed shortfall in the invoiced recovery of OPEX at that point of $70,457 for the 2014 year.

[23] The next day Mr Kenny finalised his valuation of the Property at $5,000,000 (GST exclusive). In doing so, he took account of rent and OPEX to be paid by a new tenant in the 2014 year. That additional OPEX recovery, Mr Kenny calculated, would

reduce the OPEX shortfall to a range of between, approximately, $45,000 to $50,000. Having said that, Mr Kenny went on to comment:

> [T]here is also potential for those lessees subject to more onerous liabilities to request a reassessment of their liabilities in which case, given that the under contributing portions cannot be increased, the non-recoverable OPEX could increase. It is estimated that under this scenario the shortfall could increase by a further $15,000 to $20,000.

[24] On the basis of the 21 July 2014 figures provided by Wellsford's accountants, the Group calculated the net income from the Property (rent less unrecovered OPEX) as being $362,525. That contrasted with the figure of $405,551 provided by Wellsford in the information memorandum.

[25] The Group met with Jones Lang on 23 July 2014. They told Jones Lang the conclusions they had reached based on the 21 July figures:

Gross Rent:	432,982
OPEX Recovery:	(70,457)
Net Rent:	362,525

[26] Jones Lang had not until then been aware of the 21 July figures. They consulted Wellsford. Wellsford's principals were surprised, particularly as the Group had said they were relying on Wellsford's accountants' numbers. Mr Lea, the Wellsford shareholder responsible for instructing Jones Lang, emailed the firm that day:

> These are historical numbers and do not represent the latest rents or Opex share (which Nigel Kenny had prepared!). I am a little disappointed that Garry has not checked these as I see that the Management and Admin fees are in there and this is actually part of Garry's salary as we shared his costs across the group for tax purposes.
>
> We will come back with a Sumpters reconciliation of April 2014 to date (actuals) and forecast out to March 2015 (we are already getting the rent increase from Caltex). This is the income stream that we are actually selling the business on and what we are currently enjoying.

[27] There followed further discussions between the Group and Jones Lang on behalf of Wellsford. The focus of those discussions was to narrow the gap between the two net revenue estimates. The shortfall between OPEX incurred and OPEX recovered was the key variable in arriving at the net revenue number.

[28] Wellsford's accountants were asked to review the numbers in the information memorandum. They did so. They accepted by far the larger part of the adjustments that the Group had made, based on the 21 July figures, to the net revenue figure disclosed in the information memorandum. Some minor upward adjustments from the Group's figure were identified by the accountants. After Wellsford's principals had considered the revised advice, Mr Lea advised Jones Lang on 25 July 2014 in the following terms that Wellsford would accept a net income figure of $384,200:

> If you add these [a reference to the minor uplift adjustments identified by Wellsford's accountants in their review] in, and exclude security as they may want to have someone monitor alarms, we are prepared to accept the net revenue number of $384,200 ($376,225 + $7,975). At the agreed cap rate of 7.5% this comes to $5.122m
>
> We will settle at this number

[29] Jones Lang conveyed that message to the Group.

[30] A haggle ensued, focusing on price.

(a) The Group counter-offered at $5 million, based on their original CAP rate of just under 7.6 per cent.

(b) Jones Lang replied: "I will convey. But vendor had always [sought] 7.5%. If I was you I would refrain from poking him in the eye at anything other than 7.5%."

(c) The Group came back, reminding Jones Lang that their original offer was "nearly 7.6% and accepted. We are now trying to agree on the [net] income."

(d) Jones Lang then advised "Vendor has agreed $5.1 with his partners".

(e) The Group responded: "Thanks for the offer but it is declined. I presume you know the valuation came in at $5 million. Also remember our offer hasn't changed. We are now applying the original agreed yield to their [net] rental income figures."

(f) Jones Lang replied that they would "try [the vendor] at 5.05", wanting to make sure the offer was above Wellsford's "$5.0 drop dead". The next day, 26 July 2014, Jones Lang advised that Wellsford would accept an offer of $5.05 million, but that was "the bottom line" and there were to be "no other adjustments down".

[31] At 5.07 pm on 26 July the Group confirmed they were prepared to settle at $5.05 million. That price represented an implied yield of 7.6 per cent on Wellsford's agreed net income of $384,200, or 7.2 per cent on the Group's figure of $362,525.

[32] The Agreement was declared unconditional and settlement took place on 26 August 2014.

[33] Shortly before settlement Mr Sullivan and the Group became aware that one tenant — Caltex No 8 Ltd, the owner of the service station business — had challenged the OPEX allocated to it for the financial year ending 31 March 2014, as invoiced by Wellsford and by reference to which the Group had calculated the overall OPEX shortfall when finalising its negotiations with Jones Lang.

[34] As matters transpired, Caltex No 8 had received its first wash-up invoice, for the 31 March 2014 year, on 27 May 2014 — around the time Wellsford decided to put the Property on the market. That same day Caltex No 8's finance director, a Mr Peter Hardy, emailed Wellsford's accountants asking for various maters to be explained. He wrote:

> Just a couple of quick things initially.
>
> 1. Can you please send me a copy of the budget and the detail of what has over-run so we can analyse why such a significant washup.
>
> 2. Can you please identify why we are being allocated 52% of power as we have own meter and are receiving separate accounts for our usage.
>
> 3. Can you provide the breakdown to detail on Hireage/leases and R&M — so that we can identify if tenant specific or general — they are pretty chunky numbers!

> Will have our ops manager run an eye over it as well.
>
> Thanks
>
> Pete

[35] Having spoken to Mr Hannam, Ms Foon (the accountant) replied saying she would "put some numbers together and get you something by the end of the week".

[36] After Ms Foon provided that information, Mr Hardy replied on 30 May 2014, copying in Mr Hannam:

> Thanks [Ms Foon]
>
> I will reply to both you and [Mr Hannam] however there are a number of costs on here that are inequitably allocated — some which are quite clear — (for example the suggestion that we pay 52% of the total common area power costs just for customer toilet access.)
>
> Sending this as a heads up as I believe a re-allocation needs to be done and do not want to prejudice your opportunity to recover from the other tenancies. I will provide a comprehensive reply to follow up with reference to the Lease. I suggest that given the quantum you do not finalise the invoices for other tenancies until we have had a substantive discussion, and preferably resolution.
>
> Rgds
>
> Peter

[37] Ms Foon replied almost immediately, advising Mr Hardy that "[Mr Hannam] is away on leave at the moment and won't be back until Monday 9th June". Mr Hardy responded, again within minutes:

> That's OK — will give me a chance to get a proper reply to you. Main purpose for replying quickly was so that you had opportunity to hold the invoices to other tenants if they had not gone out.
>
> Pete

[38] It was those emails, and in particular Mr Hardy's of 27 and 30 May 2014, that Mr Sullivan said should have been disclosed by Wellsford during the Group's due diligence, but were not.

[39] After settlement, the Group and Caltex No 8 entered into discussions. Eventually the OPEX issue was settled. Caltex No 8 would, going forward, pay less OPEX than had been assumed by the Group based on Wellsford's disclosed figures.

[40] The damages of $428,337 sought in the High Court by Mr Sullivan and Port Albert from Wellsford and Mr Hannam represented the reduction in the value of the Property caused by the corresponding reduction in net income from the Property, as determined at a CAP rate of 7.48 per cent.

The High Court decision

Causes of action

[41] Mr Sullivan and Port Albert pleaded four causes of action against Wellsford and one against Mr Hannam personally. The non-disclosure by Wellsford of Mr Hardy's emails meant, Mr Sullivan and Port Albert claimed, that Wellsford had:

(a) made what constituted misrepresentations by (i) silence and (ii) of fact in terms of s 4 of the Contractual Remedies Act 1979;

(b) breached its contractual obligations under cls 6 (vendor's warranties and undertakings) and 18 (due diligence) of the Agreement; and

(c) engaged in misleading or deceptive conduct in breach of s 9 of the Fair Trading Act 1986.

[42] That same non-disclosure also meant that Mr Hannam had personally engaged in misleading or deceptive conduct.

[43] We summarise Gordon J's findings in the High Court by reference to those causes of action, adopting the order in which she did so.

Breach of the Agreement

[44] The Judge explained why she considered the breach of contract claim first:[6]

> In his closing submissions [counsel for the plaintiffs] said that the third cause of action was at "the front, left and centre" of the plaintiffs' case. He placed the most emphasis on the claim for breach of contract. His position was that if the plaintiffs' claim was made out under this head, then the only other cause of action requiring consideration was the [Fair Trading Act] claim.

[45] The Judge reasoned that the proper interpretation of cl 18 was to be considered in light of the doctrine of caveat emptor. That meant Wellsford's disclosure obligation was limited to it providing information relevant to the due diligence investigation "as requested by the purchaser".[7] On the facts, the Group's inquiries regarding OPEX were not sufficient to require disclosure of the two emails.[8] They were, the Judge reasoned, both too general and at the same time too specific to have constituted a request focusing on the subject matter of those emails. Accordingly, there was no breach of cl 18. Neither was there a breach of cl 6: the emails did not constitute a "notice or demand" as those terms were to be interpreted.[9] The first cause of action failed accordingly.

Misrepresentation by silence

[46] As noted above, as part of the Group's due diligence its solicitors raised various issues with Wellsford's solicitors, including that of OPEX. The exchange as to OPEX is recorded at [14] above. Mr Sullivan argued that Wellsford's failure to disclose its exchanges with Caltex No 8 relating to the latter's OPEX allocation was, given what was said in response to the OPEX query, a misrepresentation by silence. The Judge reasoned that Wellsford's solicitors' reply was primarily directed to an historical shortfall in OPEX recoveries.[10] As to the comments about having attempted to "clarify and crystallise OPEX with each tenant", they were vague and non-committal.[11] It was,

6 High Court judgment, above n 1, at [130].
7 At [161].
8 At [165].
9 At [178].
10 At [212].
11 At [212].

the Judge concluded, "an effectively meaningless statement".[12] Taken overall, the Group had simply not asked the right questions.[13]

Misrepresentation of fact

[47] In that same letter, the Group's solicitors had inquired:

> Where the tenants are recent e.g. Caltex Wellsford Ltd and Forbidden City New Zealand Ltd — are there any disputes with the previous tenants?

[48] Wellsford's solicitors replied:

> Our client advises there are no outstanding disputes with the tenants.

[49] Mr Sullivan and Port Albert said that reply was a misrepresentation of fact because — as evidenced by the undisclosed correspondence — there was in fact a dispute with Caltex No 8.

[50] The Judge reasoned that, because the Group had asked of disputes "with the previous tenants", Wellsford's reply that there were no outstanding disputes with "the tenants" was to be construed as a statement relating to previous tenants.[14] Accordingly, there was no misrepresentation. The second cause of action also failed.

Misleading and deceptive conduct

[51] On that basis, the Judge concluded the threshold of misleading and deceptive conduct, as set by the Supreme Court in *Red Eagle Corporation v Ellis*,[15] had not been met.[16] Moreover, and as regards the claim against Mr Hannam personally, the statements had been made by Wellsford and its agents, and not Mr Hannam himself.[17] Any attempt to hold Mr Hannam personally liable for them was doomed to fail.

---

12 At [212].
13 At [213].
14 At [193].
15 *Red Eagle Corp Ltd v Ellis* [2010] NZSC 20, [2010] 2 NZLR 492 at [26]–[29].
16 High Court judgment, above n 1, at [220].
17 At [222].

Causation and quantum

[52] The Judge did not therefore go on to analyse the issues of causation and quantum of damages had any of the causes of action succeeded.

The appeal

The appellants' submissions

[53] On appeal, Mr Dale for the appellants focused on the Judge's finding that there had been no breach of the due diligence obligation in cl 18. Properly interpreted, cl 18 required Wellsford to disclose "any information relevant to the due diligence investigation". The extent of Wellsford's obligation was to be assessed objectively — given the nature and extent of the Group's due diligence investigation, had Wellsford failed to provide relevant information in its possession? The Judge had been wrong to narrow the extent of that obligation in the way she had by reference to the doctrine of caveat emptor.

[54] On the facts, Wellsford knew that the focus of the Group's due diligence was the question of OPEX, and more particularly the shortfall in the recovery of OPEX expenses that the owner of the Property would face going forward. Wellsford was therefore required to disclose the emails from Caltex No 8 in response to the very focused and specific inquiries that the Group had made. That meant it had also made the pleaded misrepresentations by silence and of fact, and had acted in a misleading and deceptive manner in terms of the Fair Trading Act. As for Mr Hannam, he had made the decision not to disclose the emails. He explained he had done so because, in his view, the emails did not raise a dispute. It was a matter for the Court to determine whether Mr Hannam's conduct in these circumstances constituted a breach of the Fair Trading Act.

[55] Mr Dale did not pursue the alleged breach of cl 6.

The respondents' submissions

[56] For the respondents, Mr Goodall supported the Judge's reasoning. Agreements for the sale and purchase of land are not contracts of utmost good faith. As the Judge

noted, the principle of caveat emptor applies so that the onus is on a purchaser to make inquiries as to matters it considers relevant.[18] Those inquiries determined the scope of a vendor's disclosure obligations. Mr Sullivan's interpretation would have the effect of turning cl 18 into a vendor's positive warranty that it had disclosed all information held relating to the property of possible relevance to a purchaser. That interpretation was inconsistent with wording the parties had used to denote warranties in other clauses of the Agreement, as well as the parties' subsequent conduct.

[57] The Group were sophisticated and experienced investors represented by solicitors and other expert advisers. They were perfectly able to make all necessary inquiries. Knowing from the outset the difficulties that existed with the determination and recovery of OPEX under the various leases, they had simply failed to make the necessary inquiries so as to give rise to an obligation of disclosure with respect to the emails of May 2014. Based on their knowledge of the unsatisfactory treatment of OPEX, including its calculation and recovery, the Group and Mr Sullivan as purchaser had assumed the risks of the uncertainty that was necessarily associated with any estimation of future OPEX recovery shortfalls.

[58] Seen in that context, the replies on behalf of Wellsford were neither misrepresentations of silence nor misrepresentations of fact. Likewise, Wellsford had not engaged in misleading and deceptive conduct.

[59] Mr Goodall also raised a number of additional reasons why the claims could not succeed:

(a) Mr Sullivan could prove neither reliance nor causation in relation to the alleged misrepresentations.

(b) Port Albert as a nominee and not a party to the Agreement could not sue on it.

(c) Because Port Albert had purchased the Property, Mr Sullivan had not suffered any loss.

---

18 High Court judgment, above n 1, at [160].

(d) The claim for damages could not succeed. The damages sought were for diminution of value. But Mr Sullivan had adduced no valuation evidence. Furthermore, there was no evidence as to actual future net income from the property.

Analysis

Overview

[60] We approach our analysis of the parties' competing contentions in the following way:

(a) We first consider the Judge's interpretation of cl 18 and her conclusion that the failure to disclose the emails did not breach the disclosure obligation. We disagree with the Judge's interpretation. We conclude that Wellsford did breach cl 18. As Mr Dale accepted, this conclusion means we do not need to consider the claims for misrepresentation.

(b) We then consider the claim under the Fair Trading Act, and whether Mr Hannam is personally liable. We conclude that Wellsford acted in a misleading and deceptive manner, and that Mr Hannam is personally liable.

(c) We finally consider remedy and the questions of causation and quantification of damages.

Clause 18 and Wellsford's disclosure obligation

[61] The Judge focused her analysis on the nature of the inquiry required by the purchaser to trigger the vendors' disclosure obligation. For Wellsford, the submission had been that a detailed and particularised inquiry was necessary. For Mr Sullivan, the argument had been that the purchaser need only identify a general scope or area of the due diligence investigation to give rise to a duty of disclosure.

[62] The Judge acknowledged that the plain language of the Agreement appeared to favour the interpretation argued for by Mr Sullivan.[19] But, referring to the doctrine of caveat emptor she reasoned:[20]

> Where, as in the present case, the contractual provision forms part of a contract for the sale of land, the doctrine of caveat emptor is relevant. The doctrine of caveat emptor means that, in general, a purchaser bears the onus of making any relevant inquiries regarding the property. The vendor, however, is not obliged to disclose any information about the property.
>
> (Footnotes omitted.)

[63] That meant cl 18(i) placed a limited obligation on Wellsford to provide information relevant to the Group's due diligence investigation, as requested by the Group.[21] That did not require Wellsford to evaluate the queries put forward by the Group to consider whether there was further information, over and above that requested, which might be relevant to their due diligence investigation.[22]

[64] In the Judge's view none of the specific questions put to Wellsford sought information regarding disputes relating to OPEX involving existing tenants.[23] It would have been a simple matter for the Group to either make a general request for all relevant information regarding OPEX, including matters relating to the recovery of OPEX from tenants, or alternatively to ask more specifically whether there were any disputes with the current tenants. Either inquiry would have given rise to the obligation to disclose the emails. In their absence, no disclosure obligation arose.[24]

[65] We disagree.

[66] Due diligence is an increasingly important feature of modern contracting processes. Due diligence takes many forms. The allocation of risk, particularly as to the accuracy and completeness of information disclosed, varies widely. To the extent that the principle of caveat emptor emphasises that it is the responsibility of a purchaser to take care, providing for due diligence can be seen as enabling a purchaser

---

19 At [160].
20 At [160].
21 At [161].
22 At [162].
23 At [165].
24 At [166].

to do just that. That is how parties to a commercial contract, such as the Agreement, understand the due diligence process. It is therefore surprising that what would appear to be the natural and ordinary meaning of the due diligence clause in the Agreement should be narrowed by reference to the doctrine of caveat emptor.

[67] The ADLS standard form agreement is a carefully drafted document. It creates a detailed contractual relationship between vendors and purchasers of real estate. It attempts to allocate risk on an objectively reasonable basis. Its very existence, together with its specific terms and conditions, reflects a significant lessening of the relevance of the principle of caveat emptor in that area.

[68] Against that background, we consider the Judge was wrong to conclude that the doctrine of caveat emptor somehow narrowed the ambit of the disclosure obligation created by cl 18(i). In the context of a carefully drafted standard form agreement, supplemented by a due diligence clause in the terms used here, the extent of the vendor's disclosure obligations are to be determined by an objective assessment of what a vendor, acting reasonably and having regard to the subject matter of the purchaser's due diligence inquiries, would determine was relevant to those inquiries.

[69] Here, the impact of unrecovered OPEX on the net revenue from the Property had become the focus of the Group's due diligence. As we have recorded in more detail above (at [13]–[31]):

(a) The Group specifically raised the issue of shortfall of operating expenses in their first due diligence inquiry on 1 July 2014. They were not satisfied with the general responses that enquiry received. Mr Kenny inquired further.

(b) What Mr Kenny sought was information that would enable the Group to arrive at a realistic projection of the OPEX shortfall. Accordingly, what he needed were the actual costs incurred.

(c) On 10 July 2014, Wellsford, in its first detailed response to the Group, responded with details including net revenue. Given that Wellsford had declined to provide its detailed financial accounts, the Group sought certified details of rents and operating expenses for the years 2012, 2013 and 2014.

(d) The provision of those figures did not, however, satisfy the Group. Because the Group were not satisfied, due diligence was extended. The Group sought further information focusing specifically on OPEX costs that were not passed onto the tenants — "the ones we have to pay". It was the figures provided by Wellsford's accountants on 21 July 2014 that finally enabled the Group to understand the position satisfactorily. After further discussion, the crucial net income figure of $384,200 was "accepted" by Wellsford for its part.

(e) The final negotiation of the purchase price then took place based on each party's view as to net rent, the appropriate CAP rate, and hence the Property's value.

[70] In that context, Caltex No 8's very clear indication that it considered the OPEX that had been allocated to it for the year ending 31 March 2014 was inequitable is material. Wellsford had communicated internally, and with Caltex No 8, on that issue on an ongoing basis.

[71] Those communications included:

(a) Ms Foon emailing Mr Hannam on 10 June 2014, noting that Mr Hardy had questioned the percentage allocation and asking Mr Hannam whether he had heard anything further. Mr Hannam replied that same day saying he had not heard and asking Ms Foon to give Mr Hardy "a nudge".

(b) That same day, Ms Foon emailed Mr Hardy, advising him that Mr Hannam was back at work and asked if Mr Hardy had any further queries on the OPEX wash-up so that they could "get them sorted sooner rather than later".

(c) On 16 June 2014, Mr Hannam and Ms Foon exchanged emails relating to the OPEX wash-up generally and the impact non-payment of those invoices was having, including as to the need for Wellsford to establish a specific overdraft facility to manage its cash flow. Mr Hannam advised Ms Foon to give Caltex No 8 "until the end of the week and bill [Mr Hardy] also".

(d) On 23 June 2014, Ms Foon emailed Caltex No 8 asking: "also what is the state of our annual OPEX washup I sent you at the end of May?" No reply was received from Caltex No 8.

[72] We conclude that a fair and objective assessment of the significance of Caltex No 8's response to the OPEX wash-up invoice was that it was challenging its liability for the amount invoiced. The references to the allocations being (i) inequitable, (ii) not supported by the terms of the lease, and (iii) likely to require adjustment of other tenants' invoices, all support that conclusion. The fact of that challenge was material, relevant information in the context of the Group's due diligence. It related directly to the issue of net revenue.

[73] To determine the scope of the disclosure obligation here by reference to matters on which very detailed and particularised inquiries were made is, in our view, commercially unrealistic. It fails to give effect, moreover, to the terms of Wellsford's disclosure obligations. Remember, the obligation of Wellsford was not only to allow "full access to the property" but also "to provide the purchaser with any information held relating to the property relevant to the due diligence investigations".

[74] We find accordingly that by not disclosing the fact of Caltex No 8's challenge to its OPEX allocation Wellsford did, as Mr Sullivan contended, breach its disclosure obligations under the Agreement.

[75] In reaching that conclusion we consider that, in terms of orthodox agency principles, there can be no question but that Wellsford, through Mr Hannam, its agents, Jones Lang, its accountants and its lawyers, was to be taken as knowing both of the issues raised by Caltex No 8 and the scope and extent of the Group's due diligence

inquiries. It is that scope and extent taken as a whole, rather than the very specific questions the Judge focused on, that for us created the context for determining relevance.

[76] We turn now to the question of liability under the Fair Trading Act.

The Fair Trading Act claims

[77] Section 2(2) of the Fair Trading Act makes clear that a failure to disclose relevant information may constitute misleading or deceptive conduct:

> In this Act, a reference to engaging in conduct shall be read as a reference to doing or refusing to do an act, and includes,—
>
> (a) omitting to an act; or
>
> (b) making it known that an act will or, as the case may be, will not be done.

[78] Omission need not be advertent.[25] Whilst the Group were experienced property investors, and knew of the difficulties and uncertainties associated with the recovery of OPEX, they had to rely on Wellsford to provide information both as to the total OPEX it incurred and as to the amount actually recovered from the tenants. Only Wellsford had that information. Wellsford's disclosure of invoiced OPEX, including Caltex No 8's wash-up invoice, without disclosing that Caltex No 8 had raised a specific challenge to its liability under that invoice was, in our view, misleading and deceptive conduct.

[79] Whether Mr Hannam is personally liable is another question. We approach this question on the basis that Mr Hannam was not acting on his own account: rather, as a Wellsford shareholder and its sole director, he was acting on its behalf. What impact does that have on his possible liability?

[80] A similar question arose in *Body Corporate 202254 v Taylor*.[26] At issue there were statements made in promotional material for a residential development that turned out to be a leaky building. Disgruntled investors represented by

---

25 Ian Gault and others (eds) *Gault on Commercial Law* (online ed, Thomson Reuters) at [FT2.01].

26 *Body Corporate 202254 v Taylor* [2008] NZCA 317, [2009] 2 NZLR 17.

the Body Corporate sued Mr Taylor, a director of the development company, and others. Mr Taylor was in effect the principal of that company and the individual behind the development. The investors' actions were in negligence and under the Fair Trading Act. Mr Taylor filed an application for strike-out on the basis the pleadings did not disclose an arguable cause of action. The High Court struck out the negligence cause of action, but not that under the Fair Trading Act.[27] Both sides appealed.

[81] This Court, having discussed in considerable detail the difficulty the negligence claim against the director personally faced but before determining the question of strike-out as regards that cause of action, considered the case against the director as pleaded under the Fair Trading Act. That case had been pleaded in two ways: against the director as himself being a person who in trade had engaged in misleading and deceptive conduct (s 9); and against the director as a party to the development company's misleading and deceptive conduct (s 43).

[82] The Court proceeded on the basis that Mr Taylor, the director, was in fact ultimately responsible for the material which was the focus of the Body Corporate's complaint.[28] It first considered Mr Taylor's possible liability under s 43. Noting that although s 43 addresses civil relief, the Court said it was significant that the subsection used the language of the criminal law, namely aiding, abetting, counselling or procuring.[29] Furthermore it was perfectly clear that the criminal tests for party liability applied. It followed that Mr Taylor could not be liable under s 43 unless he knew that the representations in the brochure were untrue. As the owners had acknowledged they would have some difficulty establishing that fact, the Court focused on the question of whether the owners had an arguable case against Mr Taylor on the basis that he was a principal.

[83] Here, there was no pleading by Mr Sullivan against Mr Hannam of party or ancillary liability under s 43. It is therefore only necessary for us to consider whether,

---

27 *Body Corporate 202254 v Approved Building Certifiers Ltd* HC Auckland CIV-2003-404-3116, 13 April 2005 and *Body Corporate 202254 v Approved Building Certifiers Ltd (in liq) (No 2)* HC Auckland CIV-2003-404-3116, 29 August 2006.

28 *Body Corporate 202254* (CA), above n 26, at [65].

29 At [66].

as was pleaded, Mr Hannam was himself a person acting in trade and whether as such he acted in a misleading and deceptive way.

[84] In *Body Corporate 202254* this Court said the answer to the possible liability of the director as principal under s 9 turned on two overlapping questions:[30]

(a) Was it arguable that the "in trade" requirement was met given that Mr Taylor was acting only as an agent and director of his companies?

(b) Was it arguable that Mr Taylor's conduct associated with the publication of the brochure was misleading or deceptive?

[85] In the course of answering the first question the Court discussed the two approaches which had been taken to the interpretation of the requirement of acting "in trade".[31] The first, which the Court called the broad approach, was that s 9 was not confined to the conduct of a person who was trading on her own account. The second, termed the narrow approach, was that if a person was not trading on her own account, she could not have been engaged in trade. The Court reviewed in detail case law and academic commentary, both here and in Australia, before concluding that the broad approach applied.[32] In doing so the Court reasoned:

> [78] At this point the issue comes down to competing policy considerations: on the one hand, consumer protection considerations which are best served by a broad approach to liability; and on the other, the undesirability of imposing unexpected liabilities on employees (along with an associated weakening of the usual protection afforded by limited liability status). Although both the broad and narrow approaches are tenable, we see no reason why we should depart from the broad approach given its congruity with the words of the statute, the most recent and authoritative Australian decision on similar legislation and, most significantly, the pattern of New Zealand authority, including judgments of this Court.

[86] Having answered the first question in the affirmative, the Court went on to consider the conduct of the director to assess whether his conduct was misleading or deceptive.[33] In discussing that point, the Court referred to a number of decisions where

---

30 At [67].
31 At [68].
32 At [78].
33 At [79].

the misleading and deceptive conduct was constituted by positive representations.[34] In such a case, the enquiry was as to the extent of the director's involvement personally with the making of the representations in question. The Court, referring to a previous decision, said:

> [82] In *Kinsman*,[35] this Court observed (at [27]):
>
> > It will be a rare case where a director who participates directly in negotiations as to his or her company's business will be able to avoid s 9 liability simply on the basis that he was acting only on the company's behalf.
>
> In that case, of course, as the passage we have cited suggests, the director had been involved in face to face negotiations with the parties to whom the key representations had been made, a situation which was quite different from that in *Megavitamins*.[36] Where a case concerns pre-contractual representations (as *Kinsman* did), the director/senior employee making the representations might be thought, by implication at least, to be inviting the other party to believe him or her, albeit not necessarily inviting reliance on his or her "pocket-book", cf the comments of La Forest J in *London Drugs*[37] at 387.

[87] Here, the misleading and deceptive conduct is not constituted by a positive representation, but by a failure to disclose. The discussion in *Body Corporate 202254* suggests that the enquiry, in general terms, is whether a person was "directly and causally involved" in the conduct of the corporate which was misleading and deceptive.[38] That is, is there a sufficient causative link between the actions of that person and the alleged misleading to enable the party misled to seek compensation under s 43?

[88] Here, and as regards the actions of Mr Hannam, in our view the answer to those questions is yes.

[89] First, Mr Hannam was closely involved with the issue of Caltex No 8's OPEX liability:

(a) It was Mr Hannam to whom Ms Foon referred Caltex No 8's 27 May 2014 initial queries regarding the "significant wash-up".

---

34 At [81]–[84].
35 *Kinsman v Cornfields Ltd* (2001) 10 TCLR 342 (CA).
36 *Megavitamin Laboratories (NZ) Ltd v Commerce Commission* (1995) 5 NZBLC 103,834 (HC).
37 *London Drugs Ltd v Kuehne & Nagel International Ltd* [1992] 3 SCR 299.
38 At [85].

(b) It was Mr Hannam who supervised the response to Caltex No 8, commenting that it was Caltex No 8's first washup invoice and, knowing those involved, they would want to understand the numbers. Ms Foon replied to Caltex No 8 that day, adding Wellsford's answers onto its original email and quoting Mr Hannam's response on one of the queries.

(c) Ms Foon liaised with Mr Hannam from the receipt of the "inequitable allocation" email of 30 May until, at Mr Hannam's instructions, she sent a new invoice to Caltex No 8.

[90] Secondly, Mr Hannam was directly involved in the sale process generally, and more particularly in the Group's ongoing efforts to clarify the position relating to the OPEX shortfall. Having said that, it is appropriate at this point to note Mr Hannam's evidence of being unwell in 2014. In his evidence-in-chief he said:

> I was diagnosed with acute multi myeloma in 2013, and underwent a stem cell implant in March of 2014. I was in isolation recovery for a period [of] three months after this procedure.
>
> I was extremely unwell during the whole of the period relating to this dispute, and for this reason was not as closely involved with [Wellsford] as I had been historically. I was sometimes unable to be contacted except for short periods by email or phone. … I was extremely unwell when the decision was made by the shareholders of [Wellsford] to sell the property, and was not closely involved in the sale to Peter Sullivan. Negotiations were conducted through John Lea, who was also responsible for providing information to [Wellsford's] agent, [Jones Lang]. I did not compile this information for the information memorandum, nor did I cause information to be disclosed on [Jones Lang's] website, or to any potential purchaser …
>
> As far as I was aware, all sale negotiations took place using [Jones Lang] as an intermediary. I did not meet or communicate with the purchaser [or its principals] directly, nor do I understand [Wellsford's] other shareholders to have met with them.

[91] Notwithstanding, in cross-examination Mr Hannam confirmed that from June 2014 onwards he did not think his judgement was impaired by his illness. He was able to respond, as the record shows, to emails whilst in hospital and by the second half of June he was out of hospital, out and about and spending short hours at work. We are therefore satisfied that notwithstanding that illness Mr Hannam's involvement in the sale was of some significance.

[92] Against that background we note the following features of Mr Hannam's involvement with the sale process generally:

(a) In a very early internal Wellsford email, dated 3 November 2013 and copied to Mr Hannam, Laurence Lowe — another Wellsford principal — commented on the significance of OPEX for the possible sale of the Property saying:

> The overall issue of OPEX apportionment (who pays for what percentage of what and when) is incredibly complicated. I had been doing multi-tenant OPEX accounts for many years and have never seen anything as complicated as this.

(b) On 20 June 2014 Wellsford's solicitors sent an email to various Wellsford principals, including Mr Hannam, discussing proposed changes to the offer that had been received from Mr Sullivan. That email included the following:

> Note Garry [Hannam] to confirm:
>
> 1. No arrears of rent or outgoings. If so, we should reserve right to collect any outstanding rental/outgoings post settlement.
>
> 2. Any works carried out by him have been consented to.
>
> 3. Building WOF up to date and compliance schedule complied with.

Wellsford's lawyers asked to see Mr Hannam later that day, no doubt to discuss matters. The evidence was unclear as to whether that meeting occurred.

(c) Mr Hannam himself signed the counteroffer on 20 June.

[93] More particularly, we note the following details of Mr Hannam's involvement in the way Wellsford and its advisers responded to the Group's OPEX inquiries:

(a) Mr Hannam was the point of contact for Wellsford's accountants, and Ms Foon in particular: it was Ms Foon who generated the specific information conveyed to the Group.

(b) Before Wellsford's accountants sent Mr Kenny rent and OPEX information on 10 July 2014, they sent the schedules to Mr Hannam for his review, and for his confirmation that it was appropriate to send that information to Mr Kenny. The accountants copied Mr Hannam the email they sent to Mr Kenny.

(c) It was Mr Hannam who agreed to provide more information on 14 July. He then instructed Ms Foon to prepare the three-year summary of rent, OPEX and net income. Ms Foon sent the figures provided on 18 July to the Group to Mr Hannam the day before, asking him whether it was okay to send those figures to the Group. It was Mr Hannam who forwarded them to Wellsford's solicitors, so they could be sent to the Group's solicitors.

(d) Mr Hannam was copied the Group's 18 July request for further information.

(e) Mr Hannam was also closely involved in Wellsford's response to the Group immediately before Wellsford accepted in large part the net income figure the Group had come up with. Mr Hannam emailed Ms Foon on the morning of 25 July 2014, asking for some final information regarding OPEX recovery. When Mr Hannam received that information he forwarded it to Mr Lowe commenting: "I don't think this makes very good reading, it certainly doesn't represent the McDonald OPEX actual contribution. Your comments."

(f) Mr Lowe and Ms Foon then exchanged emails, endeavouring to clarify matters, as Mr Lea was dealing with Jones Lang. It was that afternoon that Jones Lang advised the Group that Wellsford would accept a net revenue number of $384,200.

[94] Thirdly, and finally, in cross-examination Mr Hannam accepted he was responsible for not disclosing during the due diligence the emails that had been received from Caltex No 8 raising issues with the allocation to it of OPEX. On a

number of occasions in his evidence Mr Hannam emphasised his understanding that, because the Group had not specifically asked whether the allocation of OPEX had been formally disputed, there was no need to disclose those emails. At the same time, however, Mr Hannam acknowledged that because Caltex No 8 had not paid its OPEX wash-up invoice when due, it was in default under its lease. That had not been disclosed to the Group either.

[95] Mr Hannam also acknowledged that it was not Wellsford's practice to deal with its tenants in a very formal way, but rather directly and on the basis of long business associations. That general practice is difficult to reconcile with his reliance on there having been no formal notice of dispute on the OPEX issue.

[96] By our assessment, that narrative establishes that Mr Hannam was directly and causally involved in Wellsford's misleading and deceptive conduct. In summary he knew that Caltex No 8 had challenged its allocation of OPEX in the wash-up invoice; he knew the focus the Group had placed in its due diligence inquiries on ascertaining clarity on OPEX as incurred by Wellsford and recovered from tenants; and he decided not to disclose the fact of Caltex No 8's challenge to the Group during due diligence.

[97] On that basis, we find Mr Hannam liable for misleading and deceptive conduct under the Fair Trading Act accordingly.

[98] In doing so, we note that at the hearing of the appeal all the parties agreed that, if we did allow the appeal, we should go on and consider the question of Mr Hannam's liability, notwithstanding the fact that the Judge had not done so in the High Court because of the view she formed of Wellsford's contractual obligations. In those circumstances, we have focused on the evidence contained in the documentary record, and what that establishes, rather than endeavouring to resolve — by reference to credibility or like considerations — the inevitable conflicts that arose between and within the evidence given on behalf of the various parties.

Causation

[99] It is a necessary condition for liability for breach of contract that the breach causes the loss. Here, the breach was the failure to disclose. In a sense that failure did

not cause any loss occasioned by Caltex No 8's successful challenge to its wash-up invoice. Rather, the "cause" of that would appear to have been that — under its lease documentation — Caltex No 8 was simply not liable for the amount Wellsford had claimed. Quite properly, Wellsford noted that the Group were aware of the limitations of the lease documentation as regards the quantification and recovery of tenants' liability for OPEX. Those limitations were explicitly commented on by Mr Kenny. It would appear that they reflected the fact that, for many years, the owner of the Property and the owner of the service station business were related parties. Whatever their origin, the implications of the inadequacies of those provisions was a risk the Group had taken. We accept that was the case. But what the Group were not aware of was that the contingency reflected in the terms of the lease documentation, and commented on by Mr Kenny, had actually crystallised in Caltex No 8's case.

[100] Wellsford also argued that if there had been a "duty" to disclose — perhaps more accurately termed an obligation — then, referring to *BNZ v New Zealand Guardian Trust Co Ltd*, the scope of the duty to inform had not commonly been found to extend to protect against losses arising from some independent cause: that is where the breach merely created or preserved the circumstances in which that loss could be incurred.[39] Thus, even if Wellsford had breached a disclosure obligation, the loss claimed by Mr Sullivan would not flow from that breach. Again, the Group knew and assumed the risk of the uncertainties in the leases. Wellsford provided no warranties with respect to the recoverability of OPEX. The settlement with Caltex No 8 was a consequence of a risk assumed by the Group, and there was no causal connection between the non-disclosure of Caltex No 8's challenge to its OPEX wash-up allocation and the settlement with it nearly three years later. There had always been a prospect of Caltex No 8 disputing the OPEX allocation and, even if the emails had been disclosed, it could still have disputed the OPEX and a settlement would be required.

[101] In our view that is not an answer to Mr Sullivan's claim here. Certainly, and as we have already acknowledged, the Group did assume risks relating to what might be called the efficacy of the leases: that is, the efficiency of the commercial arrangements between Wellsford and the tenants of the property. But it did so based

---

[39] *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664 (CA) at 683.

on Wellsford's contractual obligation to disclose matters relevant to what in fact were the subject of the Group's due diligence inquiries. That Caltex No 8 could, if the emails had been disclosed, have pursued its dispute with the Group is not the point: the point is that disclosure would have given the Group the opportunity to avoid that dispute or, at least, to have made its decision to complete the purchase on an informed basis.

[102] Wellsford also asserted that in addition to voluntarily settling with Caltex No 8 in the way they did, the Group could also have sought to recover the resulting OPEX shortfall from the other tenants. They did not do so, and hence were in this way also the authors of their own misfortune. At trial, the Group explained the steps they had taken both to settle with Caltex No 8, and to deal with the flow on consequences with other tenants. The witnesses for the Group confirmed they were aware of the Group's obligation to mitigate losses arising out of Caltex No 8's OPEX dispute, including by allocating the OPEX shortfall to the extent possible to other tenants. Their evidence addressed the process they had gone through, and the commercial decisions they had reached when endeavouring to do so. Wellsford did not, in response, mount any evidential challenge — based either on the terms of the leases or the financial and commercial realities the Group faced — to the appropriateness, in the context of the duty to mitigate, of the steps that the Group took.

[103] Accordingly, the effect of the breach has to be assessed on the basis of the position as it would have been if Wellsford had disclosed the fact of Caltex No 8's challenge to the wash-up invoice.

[104] As we think is clear, both Wellsford and the Group approached the sale and purchase of the Property in a similar way. That is, as a commercial property its value was determined by the net rental income it would generate. Whilst they may have differed on the important detail of the final figures for net income, and of the appropriate yield, their general approach was the same. That, in our view, is reflected in the final negotiations. The evidence of those final negotiations also provides a basis for what would likely have ensued if the fact of Caltex No 8's challenge to its OPEX wash-up invoice had been disclosed. That is:

(a) The Group would have lowered its estimate of net revenue, and sought a purchase price of something less than $5,000,000.

(b) Wellsford would not have accepted anything less than the "drop dead" figure of $5,000,000. In those circumstances, it may well have concluded it would be better off "tidying up" the leases, and then putting the Property on the market.

(c) As evidenced by their rejection, after their estimate of net income had largely been accepted, of Wellsford's counter-offer of $5.1 million, the Group would have walked away.

[105] Thus, the failure to disclose the emails caused the Group to purchase for $5.05 million. The question becomes one of the quantification of the damage associated with that causative breach.

Quantification of loss

[106] Mr Sullivan based his damages claim on the expert advice of John Hagen, a chartered accountant. Mr Hagen's original brief of evidence, as relevant, read:

> I am advised that the final sale price was determined by negotiation between the parties, based on agreed capitalisation rate of 7.5%, which appears to be consistent with the exchange of texts referred to in the preceding sub-paragraph.[40] Those texts included express reference to an original cap rate of 7.6% in a statement from the agent in response which said "*vendor has always [sought] 7.5%*" …
>
> Given that the parties negotiated a purchase price based upon an income yield of 7.5% it is clear to me that the appropriate basis for determining any loss arising from a shortfall in recoverability of operating expenditure should be determined using the same capitalisation rate.
>
> Thus, the damage that arises from any shortfall should be determined by dividing the shortfall by 0.75 or 7.5% to arrive at the quantum of loss.
>
> (Emphasis in original.)

---

40 The documents Mr Hagen referred to were the statements of claim and defence, the solicitors' letters in July 2014, and the schedule of OPEX income.

[107] In cross-examination, Mr Hagen confirmed the approach taken in his brief, namely that the basis of his opinion was an assumption that a CAP rate of 7.5 per cent was agreed between the parties during pre-contractual negotiations. If there had been no agreed CAP rate, then he said he would determine damages by determining the implied CAP rate by "dividing the final agreed purchase price with the net revenue expected that appeared to be agreed between the parties". He confirmed, however, that if net rent was found to have been indeterminable and the CAP rate was also found to be indeterminable (that is, not agreed between the parties), it would not be mathematically possible to determine value by the method he had used.

[108] Wellsford called Stephen Dean, a registered valuer, to give evidence.

[109] Mr Dean's brief followed the form of a standard valuation for a leased property. Having described the property and its physical characteristics, Mr Dean analysed in some detail the various leases that were current. A general theme of his analysis was the uncertainty surrounding what parts of the Property were leased to each lessee. Mr Dean also noted the uncertainties relating to the lessor's right to recover OPEX, not only as affected by the uncertainties as to leased areas but also as affected by inconsistencies in the terms by reference to which OPEX was to be apportioned and recovered.

[110] In principle, Mr Dean took a similar approach to Mr Hagen. It was clear to Mr Dean that the Property was an investment property. As such, "the income that it earns [was] inevitably the key driver of value". Moreover, the prospects of redevelopment to a higher and better use were not good. On that basis, there were two principal methods by which a valuation could be undertaken:

(a) First, by the capitalisation of the net maintainable rent, "a tried and tested method that is well recognised by both buyers and sellers".

(b) Secondly, by comparison with like market sales.

[111] There were, however, very few like market sales within the Wellsford market. Accordingly, it was necessary to cast a wider net. Mr Dean did so, analysing sales not

only in the area immediately north of Auckland but also farther away. Mr Dean analysed the yields on those properties to be in the range of 5.16 per cent to 7.5 per cent. Outliers were a property in Otaki (with a yield of 9.72 per cent that Mr Dean observed as being “excessively high”) and two individual properties sold in a portfolio sale of ten service station leases (which had yields of 8 per cent and 9.5 per cent). But the average yield of the portfolio was 7.17 per cent.

[112] Commenting on some individual features of the Property, he concluded — without particular analysis — that the Property “would demonstrate a yield in the region of 8%”.

[113] As it was for Wellford and the Group in their final negotiations, the determinative question then became Mr Dean’s estimation of net revenue. To make that judgment, Mr Dean noted in cross-examination how he put to one side the uncertainties associated with the recovery of OPEX under the leases. Instead, he posited a “reasonable” approach to the allocation and recovery of operating expenses to arrive at an estimated net income of $408,866.46.

[114] We are not persuaded by Mr Dean’s choice of a yield of 8 per cent: that was not consistent with the approach of either of the parties nor, as we understood it, his own assessment of comparable sales. Nor is there any support in the lease documentation for the “reasonable” approach he adopted to the allocation and recovery of OPEX expenses. Rather, the more realistic situation was the one Mr Kenny had summarised, which Wellsford had lived with for many years, and which Mr Sullivan and the Group now had to address. What Mr Dean’s evidence does confirm, however, and as the Group and Mr Sullivan argued, is that just as capitalisation of net rent is the appropriate method for valuing the Property, so is capitalisation of the reduction in net rent reflected by the lower recovery of OPEX from Caltex No 8 the appropriate way to calculate the quantum of damages payable by Wellsford for its failure to disclose.

[115] There being no science in CAP rates, our assessment is that the midpoint of the CAP rates recognised as appropriate by the Group and Wellsford in their final

negotiations is appropriate for these purposes. That is 7.55 per cent. On that basis, we determine that the damages payable by Wellsford are $424,371.

[116] We note finally that we do not think there is anything in the points made by Wellsford with respect to the position of Port Albert as the nominee of Mr Sullivan, either resulting in Port Albert having no standing to sue or in Mr Sullivan not incurring losses.

[117] The use of a special purpose investment company to purchase investment properties is ubiquitous. So is the process whereby the party which originally enters into an agreement for sale and purchase may nominate an entity to actually buy the property on its behalf, as such an entity will not necessarily be in place when the contract is first signed. It would fly in the face of reasonable commercial practice to artificially conclude that that structure in some way precludes — to the extent required — the enforcement of the contract and the recovery of damages by reference to the position as it would have been as between the original parties to the contract if that nomination, and settlement pursuant to it, had not been made.

Summary of findings

[118] In summary, we have found that Wellsford breached its obligation to disclose material information to Mr Sullivan and Port Albert during the due diligence investigation. Wellsford is liable in contract and also for misleading and deceptive trading under the Fair Trading Act. Mr Hannam is personally liable under the Fair Trading Act.

[119] Wellsford and Mr Hannam are liable for the loss caused. In this case, we have decided that the loss is the capitalisation of the reduction in net rent caused by the lower recovery of OPEX from Caltex No 8. Using a CAP rate of 7.55 per cent, that amounts to damages of $424,371. We make orders accordingly.

Result

[120] The appeal is allowed.

[121] Judgment is entered for the appellants against the first and second respondents in accordance with [119] of this judgment.

[122] The first and second respondents must pay the appellants one set of costs for a standard appeal on a band A basis and usual disbursements.

[123] Costs in the High Court are to be determined in that Court.

Solicitors:
Stafford Klaassen, Auckland for Appellants
Marsden Woods Inskip Smith, Whangarei for Respondents