

IN THE COURT OF APPEAL OF NEW ZEALAND

**CA526/2010
[2010] NZCA 626**

BETWEEN TRUSTEES EXECUTORS LIMITED
Appellant

AND EDEN HOLDINGS 2010 LIMITED
Respondent

Hearing: 14 October 2010

Court: O'Regan P, Arnold and Harrison JJ

Counsel: R J Gordon and N K King for Appellant
No appearance for Respondent

Judgment: 20 December 2010 at 11 am

JUDGMENT OF THE COURT

- A Leave to adduce fresh evidence is granted.**
- B The appeal is allowed.**
- C The orders made in the High Court are quashed.**
- D The High Court costs order is reversed.**
- E The respondent must pay the appellant costs for a standard appeal on a band A basis and usual disbursements.**

REASONS OF THE COURT

(Given by O'Regan P)

Introduction

[1] This is an appeal against a decision of Associate Judge Bell in which he declined to make an order under s 145A of the Land Transfer Act 1952 that a caveat not lapse.¹ Counsel for the respondent, Eden Holdings 2010 Ltd (Eden), was given leave to withdraw prior to the hearing of the appeal and there was no appearance for Eden. However, the submissions filed on behalf of Eden in the High Court were before us, and we also received a memorandum from the principal of Eden, Mr Gilbertson, in which he disputed aspects of the submissions made on behalf of the appellant.

Issues

[2] The principal issue before us is whether the evidence before the High Court established a reasonably arguable case that money obtained from Trustees Executors by the fraudulent actions of a Mr Malcolm Mayer was applied towards the acquisition of equity in the property over which the caveat had been lodged, thus giving rise to an institutional constructive trust in favour of Trustees Executors. The property at issue is 43–45 Mt Eden Road, Mt Eden, Auckland (the Mt Eden property).

[3] If the answer to that question is affirmative, a second issue arises: was it reasonably arguable that the institutional constructive trust survived the transfer of the Mt Eden property to Eden? In particular, was it reasonably arguable that the

¹ *Trustees Executors Ltd v Eden Holdings (2010) Ltd* HC Wanganui CIV-2010-483-101, 12 August 1010.

conscience of Eden was affected upon its entry into the transaction to acquire the Mt Eden property?

[4] Before dealing with these issues, we set out the factual background.

Facts

[5] The caveat in issue was registered by Trustees Executors on 4 February 2010. The interest in the Mt Eden property asserted by Trustees Executors was stated in the caveat to be the following:

Pursuant to trust arising from the receipt on behalf of the registered proprietor, [Eden], of funds applied towards the acquisition of equity in the said land of which it is registered proprietor, being funds obtained from [Trustees Executors] by the deceit of Malcolm Duncan Mayer, the beneficial owner of the said Land.

[6] Mr Mayer was a mortgage broker who had a business relationship with Trustees Executors through a company, MDM Holdings Ltd. Trustees Executors argues that Mr Mayer was the architect of a large mortgage fraud scheme committed against Trustees Executors over a number of years, involving what Trustees Executors call “hydraulicling”. The fraudulent scheme involved Mr Mayer using a number of individuals and companies ultimately controlled by him to obtain almost \$50 million in borrowings from Trustees Executors.

[7] Trustees Executors relied on Mr Mayer’s own admissions about the existence of the fraudulent scheme. Mr Mayer did not give evidence in the High Court but the Judge admitted into evidence hearsay statements from two newspaper articles which appeared in the *Sunday Star Times*² in 2009 and hearsay statements made to a Mr Nottingham, with whom Mr Mayer was then associated. The first *Sunday Star Times* article was headed up “The \$50m swindler: I confess”. It began:³

Malcolm Mayer, a New Zealand representative bridge player, sips on a cup of instant coffee and admits to his part in a \$50 million loans scam.

² This evidence was also admitted by this Court in *Trustees Executors Limited v Turnbull* [2009] NZCA 574 at [22]–[29].

³ Tony Wall “The \$50m swindler: I confess” *Sunday Star Times* (Auckland, 6 September 2009).

[8] Mr Nottingham's evidence was that he was present when Mr Mayer made his admissions to the *Sunday Star Times* reporter. He said that prior to the *Sunday Star Times* interview, Mr Mayer had admitted to him that he (Mr Mayer) had controlled a large number of transactions where he had purchased a property at market value and then on-sold it to a "front person" at a significantly higher price, with that higher price being financed by Trustees Executors. Mr Nottingham said that two of the front persons, Sho Chu, Mr Mayer's partner, and Jiang Jingyi, admitted to him that they and Mr Mayer had acted dishonestly and unlawfully, and that the information that had been supplied to Trustees Executors in support of the loan applications was false.

[9] The registered proprietor of the Mt Eden property before Eden was a company called Champion Apartments Ltd (Champion). It purchased the property on 15 January 2008. On 2 December 2009, Champion entered into an agreement to sell the Mt Eden property to LJK Investments Ltd or nominee. Lance Gilbertson of Wanganui is the sole director and shareholder of LJK Investments. Mr Gilbertson said that LJK Investments had provided services to Mr Mayer and his companies by way of restructuring companies, refinancing and redeeming mortgages, and selling properties to avoid mortgagee sales. LJK Investments issued an invoice on 1 December 2009 charging Champion \$350,000 plus GST for consulting services. The heading of this invoice was:

Consulting Services to "Mayer Group" of Properties in Auckland
Re: Lance Gilbertson and Brent Clode

[10] The invoice specified charges of \$50,000 per month for October 2009 and November 2009 for consulting services undertaken during those months, and \$50,000 per month for the period December 2009–April 2010 for "Consulting Services to be undertaken from 1 December 2009 to 30 April 2010". In other words, the invoice purported to charge Champion for services provided not to Champion but to other parties associated with Mr Mayer and included a charge of \$250,000 as effectively an advance payment for services yet to be rendered. Not surprisingly, Trustees Executors questioned the genuineness of this purported arrangement.

[11] Trustees Executors says that Champion sold the Mt Eden property to Eden in an attempt to put it beyond the reach of Trustees Executors, after Mr Mayer became aware that caveats had been lodged on the titles of other properties held by entities associated with Mr Mayer. The sale by Champion to Eden was for a consideration of \$700,000. Of this \$350,000 was the “debt” created by the invoice referred to earlier. This was set off against the purchase price. The balance of just under \$350,000 was funded by a \$170,000 advance by Malkev Properties Ltd (Malkev), which was a former owner of the property and had granted a mortgage over the property securing a loan of \$300,000 plus interest. On settlement of the sale of the Mt Eden property, Malkev re-advanced some of the funds Champion had paid to it in repayment of the mortgage. Mr Mayer had previously been a director and shareholder of Malkev.

[12] On 4 December 2009, LJK Investments assigned its rights as purchaser to Eden by way of deed. No consideration is mentioned in the deed. Eden had been incorporated on 3 December 2009 with a capital of a 1,000 shares. Mr Gilbertson was the sole shareholder and director.

[13] The sale by Champion to Eden (as assignee of the LJK Investments) settled on Christmas Eve, 2009. There are mortgages registered to a solicitor’s nominee company and to Malkev. Trustees Executors does not dispute the validity of the mortgage to the solicitors’ nominee company. The caveat was registered on 4 February 2010.

Constructive trust?

[14] As is clear from the recital of the facts above, Trustees Executors does not allege that it advanced money for the purchase of the Mt Eden property by Champion. Rather, its equitable interest in the property is said to arise because the profit made from the fraudulent scheme operated by Mr Mayer through associated persons and entities was represented by the equity in the Mt Eden property.

The High Court judgment

[15] Having admitted the hearsay evidence to which we have referred earlier, Associate Judge Bell made the following factual findings:

[35] Trustees Executors Ltd has established a reasonably arguable case that:

- a) It made a significant number of substantial loans to Mr Mayer and companies, people and entities associated with Mr Mayer;
- b) Mr Mayer was instrumental in arranging those loans;
- c) In many cases, false information was presented to Trustees Executors Ltd with loan applications;
- d) Mr Mayer was involved in presenting that false information to Trustees Executors Ltd;
- e) Mr Mayer knew that the information was false;
- f) The false information was relevant to Trustees Executors Ltd's decisions to make the loans;
- g) Trustees Executors Ltd made the loans believing the false information to be true.

[36] There have been defaults under loans, but there is no clear evidence as to the amount or extent of Trustees Executors Ltd's losses.

[37] There is no evidence linking Mr Mayer's deceit with the property at 43-45 Mt Eden Road. That is, there is no evidence that any funds alleged to have been fraudulently obtained from Trustees Executors Ltd found their way directly or indirectly into the Mt Eden Road property.

[38] There is some evidence that Mr Mayer is trying to put assets out of reach of his creditors. The sale of the Mt Eden Road property may be such a transaction. Mr Nottingham's affidavit describes an offer of \$800,000 for the property made by a third party. Mr Nottingham says that Mr Mayer turned the offer down. On the other hand the sale to Mr Gilbertson's companies has irregular features:

- a) The nominal price is less than the offer from an outsider.
- b) The payment of \$350,000 for consultancy services by LJK Investments Ltd is extremely questionable. The price is high; evidence that any work of any real value was provided is scant; the credit was given when the consultancy had not been completed. The consultancy services were said to be generally for Mr Mayer and his companies. There is no explanation why Champion Apartments Ltd should be

charged for this work. There is no evidence of any work done for Champion Apartments Ltd.

- c) The true value of any consideration passing under the transaction appears considerably less than the nominal value.
- d) The assignment by LJ Holdings Ltd to Eden Holdings (2010) Ltd is not supported by any stated consideration.
- e) The sale was not an arm's length transaction. The same lawyer acted for both parties.

[39] Against that, there is evidence that since it became owner of the Mt Eden Road property, Eden Holdings (2010) has spent funds on renovating the premises.

[16] The Associate Judge recorded that the case for Trustees Executors depended on its being able to demonstrate that it was reasonably arguable that the proceeds of Mr Mayer's frauds could be traced into Champion's interest in the Mt Eden property. However, he saw the matter as falling within the law of contract because of the creditor-debtor relationship between Trustees Executors and Mr Mayer's entities. Trustees Executors argued that the Judge was wrong to do this and that it had not been a matter in issue before him on the pleadings, nor had it been the subject of submission by either party.

[17] We do not see why the equitable remedy sought by Trustees Executors against Mr Mayer, Champion and Eden in response to the fraud that it says was perpetrated by Mr Mayer should become unavailable to it because one element of the fraudulent scheme was the entry into a loan contract with Champion. Under that agreement, Trustees Executors unwittingly loaned money on a false understanding of the risk it was taking on and unaware that this was providing Mr Mayer with the ability to skim off funds for his own or associates' benefit. The effect of the Judge's decision is to confine Trustees Executors to the exercise of contractual and statutory rights against only the party with which it has a contract (Champion) and to avail itself of those rights it must rescind the loan agreement with Champion, even though it does not choose to do so. However, in the absence of argument from Eden on this issue, we confine ourselves to these comments and leave the matter for full argument in the substantive proceeding.

[18] In the High Court, counsel for Eden had conceded that in certain circumstances money that was shown to have been wrongly obtained could be traced. Counsel for Eden based that concession on the well known statement by Lord Browne-Wilkinson in the *Westdeutsche* case that stolen money could be traced in equity, and in those circumstances the proprietary interest enforced by equity arose under a constructive trust, rather than a resulting trust.⁴

[19] Counsel for Eden argued in the High Court that in order for Trustees Executors to show that it was reasonably arguable that an institutional constructive trust arose, it needed to establish that it was reasonably arguable that:

- (a) Champion (or Mr Mayer on Champion's behalf) fraudulently obtained funds from Trustees Executors;
- (b) Champion used those funds to either purchase the Mt Eden property or service the mortgage over that property, and that an institutional constructive trust arose as a result;
- (c) Champion (by Mr Mayer or otherwise) sold the property to Eden which had knowledge of the fraud and that the transfer was not a bona fide transfer.

[20] The argument for Eden in the High Court was that Trustees Executors could not establish those matters, particularly if it succeeded in contending that much of the evidence proffered by Trustees Executors was inadmissible and should not be considered. We did not have argument before us on the evidence admissibility issue but we are satisfied that the Associate Judge was right to admit the evidence on which Trustees Executors relied in the High Court.

[21] Because of the approach we take to the case, we do not deal in detail with the High Court decision.

⁴ *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669 (HL) at 715–716.

Fresh evidence

[22] Trustees Executors sought leave to adduce further evidence in support of its appeal. This new evidence was an affidavit from Mr Russell, the head of corporate services for Trustees Executors. The evidence referred to material which has been discovered in an associated case involving Trustees Executors and Mr Mayer.⁵ That case relates to a property in Mountain Road, of which the registered proprietor was a Ms Davidson, the sister of Mr Mayer's ex-wife. In that case Associate Judge Gendall had ordered that the caveat placed over the title of the property by Trustees Executors not lapse. The litigation then proceeded to the discovery stage, and Mr Russell's evidence was that the material obtained by Trustees Executors in discovery had confirmed that proceeds of loans made to entities associated with Mr Mayer by Trustees Executors had ultimately been paid to Ms Davidson. Thus, in the case of the Mountain Road property, there was now evidence of a direct link between the loans made by Trustees Executors as a result of Mr Mayer's fraudulent scheme and the obtaining of money by an associate of Mr Mayer for his or her personal benefit or, more likely, for Mr Mayer's own benefit.

[23] Mr Russell expressed the view that if Trustees Executors could obtain full discovery against Eden in this case, it would similarly be able to obtain independent banking records showing the flow of money generated by the fraud into the Mt Eden property.

[24] We are satisfied that this evidence is fresh and cogent and we give leave for it to be adduced in support of the appeal.

Was there an institutional constructive trust?

[25] Based on the Judge's findings we are satisfied that it is reasonably arguable that Mr Mayer participated in a fraudulent scheme which involved the obtaining of loans from Trustees Executors to entities associated with Mr Mayer. The Judge's

⁵ *Trustees Executors Ltd v Davidson* HC Wellington CIV-2010-485-2471, 22 March 2010.

factual findings outlined above and the clear admission by Mr Mayer in the *Sunday Star Times* articles make this clear.

[26] We are also satisfied that it is reasonably arguable that some of the proceeds of this fraud were invested by Mr Mayer through entities and persons associated with him in properties. Mr Mayer specifically said in one of the *Sunday Star Times* articles that he had pumped the money obtained by his fraudulent activity into properties.

[27] The question then is whether there is evidence which provides a basis for concluding that it is reasonably arguable that some of the proceeds of the fraud were used to purchase the Mt Eden property. The Associate Judge found there was no link between Mr Mayer's deceit and the Mt Eden property. We differ from the Associate Judge on that aspect of the case.

[28] The evidence was that Champion had borrowed \$4 million from Trustees Executors (with Ms Chu as guarantor) pursuant to a loan agreement executed in February 2007. This loan was made to enable the purchase of a property in Robert Street, Ellerslie, Auckland, and was to be secured by a first mortgage over that property. This advance was made against a representation that the property was being purchased for \$7,700,000. That was not true. The evidence was that Mr Mayer's modus operandi allowed the properties to be purchased with the loan money funding 100 per cent of the purchase price, with additional money left for Mr Mayer to "skim off the top" for his personal benefit. Much of the income from the properties was then diverted to Mr Mayer's personal benefit as well, instead of being used to service the loans to Trustees Executors. This money was, in Mr Mayer's words, pumped back into properties.

[29] There was evidence that Champion did not own any properties other than the Robert Street property and the Mt Eden property. The transaction involving the purchase of the Robert Street property was said to have involved a swap of two apartments in Vincent Street, which records show were not in fact owned by Champion, but were held in the name of Ms Chu (Mr Mayer said that these were held as trustee for him). The swap did not occur, as the Associate Judge found.

[30] The Mt Eden property was purchased in January 2008. The Mt Eden property previously being held in the name of two companies controlled by Mr Mayer, and the transfer to Champion occurred simultaneously with an earlier transfer from one of those companies, Malkev, to Ling Yang, immediately followed by a transfer from Ling Yang to Champion. There was no evidence as to what resources Champion had to perform its obligations in purchasing the Mt Eden property. The inference which Trustees Executors asked us to draw was that the proceeds of the fraud involving the Robert Street property were used by Champion in relation to the purchase of the Mt Eden property.

[31] In our view the evidence of Mr Mayer's modus operandi in the new evidence submitted to this Court,⁶ the evidence relating to the Robert Street property and the fact that no other source of funding for Champion has been identified provides a proper factual basis for a finding that it is reasonably arguable that the proceeds of the fraudulent activity of Mr Mayer were used to fund Champion to purchase the Mt Eden property and are therefore represented by any equity available in the Mt Eden property.

[32] We find, therefore, that Trustees Executors has established that it is reasonably arguable that Mr Mayer/Champion obtained money by fraud from Trustees Executors and used those funds to purchase the Mt Eden property. The prerequisites for the creation of an institutional constructive trust, as identified by Edén in the High Court⁷ are satisfied.

[33] We are conscious that the Associate Judge said in his judgment that Lord Browne-Wilkinson's dictum in *Westdeutsche* cannot be applied in New Zealand to contracts induced by fraud. We accept that there is controversy about the ability to trace stolen money in equity. However, in the absence of any argument to this effect from Edén, whether in this Court or the High Court, we propose to do no more than satisfy ourselves that it is reasonably arguable that the requirements for a declaration that an institutional constructive trust exists are satisfied.

⁶ See [23]–[24] above.

⁷ See [19](a) and (b) above.

[34] In *New Zealand Limousin Cattle Breeders Society Inc v Robertson*,⁸ Somers J expressed the view (obiter) that where stolen money is used to acquire or improve the thief's home, that would give rise to an equitable interest in the home in favour of the victim of the theft. We apply that dictum to the facts of this case. We consider that where money has been obtained by fraud, the conscience of the perpetrator of the fraud has been affected and there is a direct link between the money obtained by the fraud and the property in respect of which the trust is said to apply. In such a case it is at the least reasonably arguable that an institutional constructive trust exists.

[35] We are satisfied that it is reasonably arguable that:

- (a) Mr Mayer obtained money by fraud from Trustees Executors and that Champion was either acting as a front for Mr Mayer or at least inextricably involved in that fraud;
- (b) An institutional constructive trust arose when Champion obtained money from Trustees Executors as a result of that fraud;
- (c) Champion applied the money to which the trust applied to the purchase of the Mt Eden property and the institutional constructive trust then applied to Champion's equity in that property.

[36] We therefore resolve the first issue in favour of Trustees Executors. However, we emphasise that we have not had argument from Eden in this Court on the requirements for the establishment of an institutional constructive trust and we do not intend our conclusion that it is reasonably arguable that such a trust exists in the circumstances of this case to bind the High Court when the case comes before the Court for substantive argument.

⁸ *New Zealand Limousin Cattle Breeders Society Inc v Robertson* [1984] 1 NZLR 41 (CA).

Did the institutional constructive trust survive the transfer of the Mt Eden property?

[37] We consider that the circumstances of the transfer of the Mt Eden property to Eden and the creation of the mortgage to Malkev⁹ provide a sufficient evidential basis for an arguable inference that Eden was not a purchaser in good faith and that it knew of the fraud of Mr Mayer and Champion. We are satisfied therefore that it is reasonably arguable that Eden now holds its equity in the property as trustee for Trustees Executors under the institutional constructive trust.

Result

[38] We allow the appeal. We quash the orders made in the High Court. We order that caveat 8407148.1 not lapse. The application to adduce fresh evidence is granted. We reverse the High Court costs order and award costs for a standard appeal on a band A basis and usual disbursements to Trustees Executors.

Solicitors:
Buddle Findlay, Wellington for Appellant

⁹ See [9]–[13] above.