IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2014-404-445
[2014] NZHC 704

BETWEEN	MIDGEN ENTERPRISES LIMITED Plaintiff
AND	STEWART MORGAN First Defendant
	WATER GUARD NZ LIMITED Second Defendant

Hearing: 4 April 2014

Counsel: D W Grove for Plaintiff
M J Fisher and L Hui for Defendants

Judgment: 9 April 2014

JUDGMENT OF FOGARTY J

This judgment was delivered by me on 9 April 2014 at 4.30 p.m., pursuant to Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Date: .....

Solicitors: Dawsons, Auckland
Castle Brown, Auckland

The narrative of undisputed events

[1] The plaintiff sold its business as a distributor of water filters and accessories to the second defendant, a company formed for the purchase, whose principal is the first defendant, Mr Morgan. The sale was by a contract dated 16 September 2013. The total purchase price was $440,000 plus GST. Prior to the completion of the purchase, the plaintiff vendor had ordered stock to a total value of $500,000 approximately. The agreement had a special clause (cl 20) relating to the stock:

> It is agreed between the parties that all stock already ordered but not received by the possession date and partially paid for by the vendor, shall be paid off by the vendor and stored by the vendor at Now Couriers with the storage cost being borne by the purchaser.
>
> The stock will be sold to the purchaser at cost plus 5% with the purchaser agreeing to purchase stock from the vendor exclusively over any purchases from other sources. The purchasers will place a maximum of one order per month from the vendor. All product will be purchased prior to 28 January 2015.

[2] The stock was acquired from a company called Cynortic Limited (Cynortic). The plaintiff vendor had an exclusive distribution agreement for New Zealand and all Pacific Islands from Cynortic. This gave the plaintiff exclusive marketing and sales rights to the Water Guard filtration system and associated products for a period of ten years with a right of renewal at the option of the plaintiff for a further ten years at no cost. The stock was provided by Cynortic and it is made up of fully complete filtration system units.

[3] The purchaser took possession on 5 November 2013. Early into the agreement in November, Now Couriers advised that they did not want to continue holding the stock and suggested that this service be provided by another related business, Online Secure Distribution facility. Mr Midgen, the principal of the plaintiff, contends that at a meeting attended by himself, Mr Morgan for the purchaser and Mr Quill of Now Couriers, it was agreed that the stock could be transferred to Online Secure Distribution but without reaching an agreement as to when the transfer would take place.

[4] On 6 February 2014, Mr Midgen sent an email to Mr Morgan:

> We understand from Now Couriers that you are planning to move the stock from their warehouse. Are you planning on paying for the stock removed or, if not, can you please provide evidence of insurance to cover the stock at the new location as well as how many units will remain at Now and how many are being transferred?

[5] The next day, the 7th of February, Mr Morgan emailed Mr Midgen:

> In regard to the stock that has been moved to 24B Fremlin Place, Avondale because, as you know, Now Couriers required an alternative and the East Tamaki option did not work out.

24B Fremlin Place, Avondale is the place of business of the second defendant purchaser, so Mr Midgen must have understood from the outset that all the stock had been moved to the defendant's.

[6] By this point in time there had been correspondence passing between Mr and Mrs Midgen and Mr Morgan, beginning on 5 January, in which Mr Morgan was expressing concern about the purchase. His opening sentence on 5 January was this:

> I am very unhappy with the Water Guard business purchase, what I paid and what I didn't get.

The letter ran for three paragraphs and ended:

> I would like you to set right these issues or buy back Water Guard New Zealand Limited from me.

[7] Then followed the email of 7 February that I have just referred to and a meeting on 11 February attended by Mr and Mrs Midgen and Mr Wayne Cameron, a business consultant assisting Mr Morgan. There was a file note prepared by the Midgens of that meeting which gave no indication of any concern over the location of the stock.

[8] At the end of that meeting, however, Mr Cameron handed Mr and Mrs Midgen a letter headed "basis for a statement of claim". This was a nine-page document expanding significantly on the letter of 5 January. It opened with this paragraph:

> The combination of "numerous events" subsequent to 1 November 2013 settlements (details emailed 5th January 2014), have forced Stewart (Morgan) to believe he has purchased the business that does not have any goodwill,

and to that end, has in a 22nd January meeting at the Midgens' house offered to sell the business back, as the "cleanest" way to resolve the issues.

[9] On 14 February at 5.00 p.m. Mr Midgen sent an email to Mr Morgan beginning:

> We are disturbed at your continuing untenable claims and your unsupportable unilateral actions (both taken or, currently, threatened).
>
> ...
>
> Please note these two immediate matters of great concern.
>
> First, vendor warranty obligations. ...
>
> Secondly, our stock. We cannot accept that you can determine the location and sole control of our stock, nor your ability to cannibalise new units for parts.
>
> Please be advised that we must re-take effective control of our stock and are making arrangements for transfer late next week to a site of our choice and under our direct physical control. Your active assistance at that time will, of course, be required.

[10] This received a reply at 6.44 p.m. as follows:

> Dave (Midgen),
>
> I think you will need to involve your solicitor in this. It's probably better that from this point forward all communication goes through them. My solicitor is Pat Castle of Castle Brown, tele 307-7054. And no I do not agree to you moving the stock; it is secured on private property and the owner does not give you permission to enter this property.
>
> Stewart (Morgan)

[11] I am satisfied this was a refusal by Mr Morgan to release the stock on behalf of the second defendant. The second defendant has maintained this position down to the hearing.

Application for interim mandatory injunction

[12] The plaintiff has applied for an interim mandatory injunction requiring both defendants to return all the stock taken from Now Couriers and returning it to Robert Pascoe Carriers Limited (Pascoe Carriers), also in South Auckland. The plaintiff

alleges that the stock has been converted and that they are likely to suffer significant prejudice in the circumstances if the stock is not returned forthwith.

[13] The application for interim injunction follows upon the statement of claim. In the statement of claim, the plaintiff alleges that in early December 2013, at a meeting between Mr Midgen and Mr Morgan at the premises of Now Couriers, it was agreed that the stock located at Now Couriers would be moved to Pascoe Carriers and held there pursuant to the terms of cl 20. (That meeting is not covered in the narrative, and is disputed.) That the removal of the stock by the first and second defendants to the premises where the second defendant trades was taken without the authority of the plaintiff and in breach of the agreement.

Position of the defendants

[14] The defendants say:

(a) That there is no evidence to support the plaintiff's pleading that the parties had agreed that the remaining stock located at Now Couriers be moved to Robert Pascoe Carriers;

(b) That there is no evidence to support an agreement between the parties as to the terms on which an alternative logistics provider would provide storage and distribution services in relation to the stock;

(c) That the second defendant was entitled to store the stock (and implicitly move it) to where it is presently stored because there is an implied term in the agreement between the parties to the effect that:

> In the event Now Couriers should not be able to continue to supply storage and distribution services, the stock may be moved to an alternative storage location provided that legitimate interests of each party should be reasonably safeguarded.

[15] The defence also argues that Mr Midgen's conduct, recorded above, prior to him taking objection to the movement of the stock supports the implication of such a term and shows that he was not initially concerned about the relocation of the stock.

[16] In the course of oral argument, both counsel agreed that Now Couriers released the stock on the instructions of Mr Morgan and that the stock is owned by the plaintiff. There is a qualification that Mr Fisher, counsel for the defendants, argues that it is by the terms of the agreement for sale of purchase, however, under the joint control of purchaser and vendor. Both counsel seem to accept that the plaintiff's concern about the defendants' control of the location of the stock emerged as the Midgens grasped the full dimensions of the dispute first raised on 5 January and then elaborated on in the basis of a claim document delivered at the end of the meeting of 11 February, but not fully absorbed until some days later; all of which being at a time before the lawyers were involved.

[17] In addition to the contention that the plaintiff acquiesced in the movement of the stock, at the prompting of the Court, the defendants volunteered an undertaking to extend to final resolution of this dispute in these terms:

> In the event that the second defendant should give notice of cancellation of the sale and purchase agreement dated 16th September 2013 (ASP) between Water Guard New Zealand Limited as vendor and Morgan or nominee as purchaser on the file proceedings or take steps in this proceeding to seek an order of the Court concerning the ASP both defendants irrevocably undertake to permit the plaintiff to take possession of the stock immediately and to store it at a location where the second defendant at its election continue to purchase items of stock as contemplated under the ASP. In the latter circumstances the second defendant agrees to pay for the third party storage and logistics costs provided that such costs are no more than the cost previously charged for such services by Now Couriers.
>
> This undertaking which is without prejudice to any claims for damages by the second defendant to the plaintiff.

[18] Following the hearing, with leave granted at the hearing, counsel for the defendants filed a more detailed undertaking. I have analysed that undertaking paragraph by paragraph and concluded that it is spelling out what is implicit in the formal undertaking granted by counsel at the hearing. For example, it says the second defendant will not continue to retain possession of any item of stock unless it intends to use that item of stock in connection with the conduct of the second defendant's business. Under no circumstances will the first defendant or the second defendant claim any lien of any kind or equitable interest or proprietary or other interest in the stock (which has not been paid for).

[19] Not surprisingly, the memorandum from counsel for the plaintiff does not accept that this more detailed undertaking resolves its concerns in any way. I have disregarded the other material from the plaintiff and agree with the defendants' submissions in reply that these submissions were beyond the scope of the leave.

Resolution

Is there a serious question to be tried?

[20] There is a serious question that the defendants converted the plaintiff's goods to their own use or detained them against the wishes of the plaintiff as owner, either when transferring the goods on 7 February or when refusing on 14 February to release them. There is no doubt that on both occasions the conduct was deliberate. There is no doubt that on the second occasion there is no suggestion that the plaintiff is acquiescing in the transfer of the goods.

[21] In support of my judgment that there is a serious argument, I refer to the facts set out in the narrative and emphasise the value of the stock, more recently calculated by the defendants to be in the order of $481,000. The reason advanced by the defendants for the stock being stored on their premises is that that lowers their cost of paying for storage. But under the terms of the ASP, they agreed to pay the costs of storage. They are not entitled to take steps to eliminate that cost under the ASP. That cannot be a justification for retaining the goods against the request by the owner to remove them. They have no basis for any lien over the goods. In that regard, their counsel has also volunteered that they would record in the undertaking that they have no basis now or in the future to a lien over the goods.

[22] So on what basis are they asserting the right to continue to retain possession of stock owned by the plaintiff? It is the implied term referred to above. That implied term will be difficult to sustain in a context where the party holding the stock does not own it and is endeavouring to escape the contract and attain a refund of a purchase price of approximately $400,000, which broadly equates the value of the stock he is holding. Implied terms are always essentially reasonable terms, reasonable in the context of a relationship between the parties. Terms which both parties can be presumed to have agreed on, before their breach.

[23] I consider that the defendants have a very weak argument in favour of the implied term and, to the contrary, I think that the plaintiff has a strong argument that the stock of the business has been converted or is being unlawfully detained.

Where does the balance of convenience lie?

[24] The plaintiff is very concerned that the second defendant would not be able to meet any judgment for damages. The plaintiff says that the second defendant was fully funded by bank advances to enable it to complete the purchase. Thus far the first defendant has not volunteered to indemnify any liability of the second defendant and it is possible, of course, that the first defendant may be personally liable for the conversion or detention of the goods if that is proved.

[25] There were competing arguments for the preservation of the status quo. As usual, the plaintiff argues that the status quo was storing the goods on behalf of the owner, not storing the goods on behalf of both parties. The defendant argues that the status quo is the safe and secure storage of the goods on the defendants' premises. In my view, the status quo is the former, for the latter asserts a control over stock which the vendor did not grant in the contract of sale and purchase, and which was wholly against its interest to grant to a dissatisfied purchaser.

[26] If the injunction is granted, it can be in terms that put the defendants in essentially the same position as they were in under the contract. Counsel advise me that Pascoe Carriers is in the same location, South Auckland, as Now Couriers. The plaintiff has asserted that the cost of Pascoe Carriers storing and releasing the goods are, for all practical purposes, the same as those which were agreed to be paid under the contract when the storage was at Now Couriers so that the grant of the mandatory injunction would put the parties back in the same position they were in, in respect of storage, for all practical purposes as agreed in the contract.

[27] I turn to the question of uncompensatable disadvantages to each party, depending on whether the injunction would be granted. In his written submissions, Mr Grove argued:

> If the goods are not returned, they are in the complete and utter control of the defendants. The plaintiff has not even been allowed to inspect his goods … It must be apparent that Mr Morgan will use these disputes, which are vigorously denied by the plaintiff, for economic advantage by way of its unlawful theft of the plaintiff's stock.

[28] Mr Morgan has signalled his intention to litigate numerous issues arising from the agreement for sale and purchase. Mr Midgen does not accept there is any basis for a claim against him. What seems clear is that the defendant has attempted to obtain economic advantage by way of a conversion and are now holding Mr Midgen to ransom.

[29] Both parties are reserving their position as to cancellation of the contract on the part of Mr Morgan and the second defendant or the plaintiff accepting the defendants' conduct as repudiating the contract on the part of the plaintiff. The position of Cynortic needs to be kept in mind at all times. Cynortic has an ongoing interest in the sales of its products throughout New Zealand and the Pacific Islands. It has sold the Australasian business to a new company controlled by the Soloman family. They have the same interest.

[30] The plaintiff faces a real risk that the breakdown in relationships between the plaintiff, as owner of half a million dollars worth of stock, and the first and second defendants, as purchasers of a distribution agreement, will result in one way or another in the stock being stranded and not available to be released to meet the demands of persons purchasing the Cynortic water filtration units. Should that happen, there is a very serious risk that the first and second defendants will not be able to satisfy an award of damages against them in favour of the plaintiff for the loss of value of these units and other associated losses.

Overall sense of justice

[31] Moving to the ultimate issue as the Court's overall sense of justice. This Court is of the view that, so far as possible, the parties should be put into the position they were in when they signed the agreement for sale and purchase, and allow the dispute as to the sale to be mediated, arbitrated or litigated. This means that the

stock should be in the possession of a reputable distributor and, so far as possible, the costs of distribution to be borne by the defendants should be the same.

[32] Accordingly, this Court orders the following mandatory injunction:

(a) The first and second defendants will allow the plaintiff, by contractors, to remove all the stock held on their premises, at the plaintiff's expense for now.

(b) The plaintiff will meet, for now, any proven difference in cost to the second defendant by reason of the charges of Pascoe Carriers, compared to Now Couriers, and additional distance costs, pending final resolution of the dispute between the parties.

(c) The plaintiff's costs in (a) and (b) are without prejudice to a final judgment of this Court.

[33] Leave is reserved to apply to the Court to establish a procedure if the parties cannot agree on a method of comparing the costs of Pascoe Carriers against Now Couriers or distance costs.

[34] The plaintiff is entitled to costs on a 2B basis. Leave reserved to either party to apply to the Count to resolve any dispute as to quantum, in which event submissions are limited to five pages, exchanged in draft.