

National Insurance Corporation

Appellant

v.

Winmark Limited

Respondent

FROM

**THE COURT OF APPEAL OF
THE EASTERN CARIBBEAN (ST LUCIA)**

JUDGMENT OF THE LORDS OF THE JUDICIAL
COMMITTEE OF THE PRIVY COUNCIL

Delivered the 16th March 2009

Present at the hearing:-

Lord Hoffmann
Lord Rodger of Earlsferry
Lord Carswell
Lord Brown of Eaton-under-Heywood
Lord Mance

[Delivered by Lord Hoffmann]

1. Winmark Ltd (“the company”) is a St Lucia company which carried on business in Gros Islet. On 7 February 2001 it granted fixed and floating charges over its assets and undertaking to the Caribbean Banking Corporation Ltd (now RBTT Bank Caribbean Ltd and hereafter “the bank”) to secure repayment of an advance of EC\$12.7m and the interest due thereon. The fixed charges included a hypothec over land in St Lucia which was duly registered in the Land Registry.

2. The company defaulted on its obligations under the loans and on 1 October 2004 the bank appointed a receiver. At that date the company

was in arrear with its payments of contributions due under the National Insurance Corporation Act 2000 (“the Act”) in respect of its employees. On 1 February 2005 the National Insurance Corporation, the body established under the Act to administer the National Insurance Fund, commenced proceedings against the company to recover EC\$505,564.19 arrears of contributions and a surcharge for late payment. There is no dispute over the amount due. The question is whether the Corporation’s claim takes priority over the bank’s rights under its hypothec over the company’s property.

3. The answer depends upon the meaning of section 74 of the Act:

“(1) Where—

- (a) any execution has been levied against the property whether movable or immovable, of an employer, in respect of a judgment against him or her, and any such property has been seized or sold or otherwise realised in pursuance of such execution; or
- (b) on the application of a secured creditor, the property, whether moveable or immovable, of an employer has been sold,

any sums due as contributions by such employer shall rank as a privileged debt *pari passu* with state taxes without the necessity for registration thereof.”

4. The term “privileged debt”, like the term “hypothec”, indicates that the background against which this provision was framed was the civilian property law of St Lucia, contained in the St Lucia Civil Code, which was based upon the Civil Code of Lower Canada of 1865 and indirectly upon the Code Napoléon. Section 74 must therefore be interpreted in the light of the provisions of the Code and the general principles of French law relating to security interests in land: see *Polinere v Felicien* [2000] 1 WLR 890, 893.

5. Article 1876 of the Code provides that “in the absence of any cause of preference”, the creditors share *pari passu* in the property of the debtor. Article 1877 says that the “legal causes of preference are privileges and hypothecs”. When section 74 of the Act describes the liability to pay contributions as a “privileged debt”, it is clearly creating a privilege within the meaning of article 1877 of the Code. Equally clearly, the bank has a hypothec. So the question is which has priority over the other.

6. The general principle is stated in Bell, Boyron and Whittaker, *Principles of French Law* (2nd ed) at p. 291:

“Certain individuals are preferred creditors and thus have legally protected *privilèges*. These entitle the individual to payment (in competition with others having similar rank) in preference to secured creditors such as the holders of hypothecs.”

7. Prima facie, therefore, the privileged debt takes priority to the hypothec. But, as the authors point out, this rule may be displaced by a requirement of registration. In France, by a *décret* of 1955, *privilèges* over immovable property were converted into *hypothèques légales* which required registration to retain their priority. A similar (if slightly more limited) reform appears to have been introduced in Québec when a new Civil Code was adopted in 1994. An amendment to article 1989 provided that—

“...Notwithstanding any provision to the contrary, no privilege of the Crown or of an agent of the Crown shall rank ahead of that of the vendor of an immoveable, or ahead of a hypothec, unless it was registered before the sale or hypothec.”

8. The purpose of this reform was explained by M. Gaspar Côté in a paper in *The Harmonisation of Federal Legislation with the Civil Law of the Province of Quebec and Canadian Bijuralism*, Collection of Studies, Ottawa (On), Department of Justice Canada, 1999, pp. 449-479:

“[It] was obviously a response to the need to end abuses resulting from the immovable privileges created by special statutes. In this regard, the report on the Civil Code of Québec prepared by the Civil Code Revision Office states that over the last one hundred years the Québec legislature had created, by special statutes, some two hundred privileges other than those prescribed in the Civil Code in favour of either the Crown or certain special corporations such as municipalities.”

9. The need for these reforms in France and Québec reinforces the general statement in *Bell, Boyron and Whittaker* that prima facie a privilege takes priority over a hypothec. In St Lucia, article 1903 of the Code enumerates privileged claims upon immovables and the order in which they rank. At the head of the queue are law costs and expenses incurred for the common interest of creditors. Then come, in order of priority, funeral expenses and expenses of the last illness, advances for

certain agricultural purposes, municipal and local taxes, the claims of a builder (subject to certain procedural requirements), the claims of a vendor, the salaries and wages of “managers, overseers and servants” for up to three months, and the wages of “labourers” for up to one month.

10. The Eighteenth Book of the Code deals with the registration of real rights, which include both privileges and hypothecs over immovable property. The general principle in article 1967 is that all real rights take effect on registration. But article 1969 provides that certain specified privileges (law costs, municipal and local taxes, salaries and wages) are “exempt from the formality of registration”. The effect of exemption appears from article 2011:

“Privileged rights which are not subject to registration take precedence according to their respective rank...Except the above cases...real rights rank according to the date of their registration.”

11. The St Lucia system for the priorities of real security rights over immovable property is therefore clear. Prima facie, a privileged debt takes priority over a hypothec and privileged debts rank inter se according to the order of priority established by article 1903, as supplemented by other legislation. But this prima facie rule has in many cases been displaced by the requirement of registration, which may result in a registered hypothec or inferior privileged debt taking priority over a registrable but unregistered privileged debt.

12. Section 74 deals with the rank of a claim to contribution in the list of privileged debts by providing that it shall rank “pari passu with state taxes”. To find out where that puts contributions on the list, it is therefore necessary to see where state taxes come. That appears in section 121 of the Income Tax Act, which says that such unpaid tax—

“constitutes a privileged debt due to the Government carrying a privilege over all property whether movable or immovable, ranking immediately after law costs and in priority to all other privileged claims, charges or debts against such person.”

13. Claims to contribution therefore share this privilege, being treated as inserted into the article 1903 list (as a notional item 1A) immediately after law costs. There is, however, nothing in section 121 to include state taxes in the list of article 1969 privileges which are “exempt from the formality of registration”. On the contrary, section 121 (2) provides that a certificate from the Comptroller as to the amount of tax due shall take effect as if it were a judgment and be registrable as such in the Land

Registry or Registration of Deeds. The priority of the privilege for state taxes therefore requires registration and, under article 2011 of the Code, takes effect from the date of registration. As it happens, the Comptroller issued a certificate in this case on 9 November 2004 in respect of EC\$384,749.20 unpaid PAYE deductions and penalties, which was registered in the same day.

14. Section 74, on the other hand, says that the privilege for contributions shall rank as a privileged debt, with the stated priority, “without the necessity for registration thereof.” It therefore retains its high rank in the list of privileges and takes priority over all other privileges and hypothecs, whether registered or not.

15. It was for these reasons (rather more succinctly stated) that Master Cottle had little difficulty in holding that the Corporation’s claim took priority over the bank’s hypothec. His decision was, however, reversed by the Court of Appeal, where the only substantive judgment was given by Rawlins JA.

16. Before the Court of Appeal, the receiver (on behalf of the bank) submitted that the privilege could not give the Corporation priority in respect of the proceeds of sale of the hypothecated property because the effect of the hypothec was that, at any rate when the property was sold, the proceeds were not the “property...of an employer” within the meaning of section 74. The proceeds were beneficially owned by the bank. This argument was repeated before the Board, both by Mr Guthrie QC for the receiver and by Mr Du Boulay, who followed him.

17. In support, counsel for the receiver relied upon statements in the House of Lords in *Buchler v Talbot* [2004] 2 AC 298 on the effect in English law of the crystallisation of a floating charge. At p. 309, Lord Hoffmann said:

“29. When a floating charge crystallises, it becomes a fixed charge attaching to all the assets of the company which fall within its terms. Thereafter the assets subject to the floating charge form a separate fund in which the debenture holder has a proprietary interest. For the purposes of paying off the secured debt, it is his fund. The company has only an equity of redemption: the right to retransfer of the assets when the debt secured by the floating charge has been paid off. It is this equity of redemption which forms part of the fund held on trust for the company's creditors which arises upon a winding up.”

18. Likewise Lord Millett said at p. 313:

“51. ... Assets subject to a charge belong to the charge holder to the extent of the amounts secured by them; only the equity of redemption remains the property of the chargor and falls within the scope of the chargor's bankruptcy or winding up.”

19. These statements were made to explain why, if in principle the costs of realising a fund should be borne by the creditors interested in that fund, it would be wrong to make assets in the hands of a receiver, which were subject to a floating charge, bear the costs of a liquidator realising assets for the benefit of unsecured creditors. As Lord Millett explained at p. 311:

“41. As formulated, the question appears to be concerned with priorities. But the real question is whether the expenses of a winding up are payable out of charged assets at all. If they are, there is no doubt that they are payable in priority to the claims of the charge holder. If they are not, questions of priority do not arise.”

20. In their Lordships' view it is dangerous to apply notions of the separate beneficial interests of the chargee and the unsecured creditors, which were used in *Buchler's* case to explain why one fund should not have to bear costs attributable to the realisation of another, to the very different question of priorities under the civilian system of security interests in immoveable property applicable in St Lucia.

21. Their Lordships consider that it is clear from the Code that neither a privilege nor a hypothec displaces the debtor's ownership of his immovable property. A privilege is only “a right which a creditor has of being preferred to other creditors” (article 1878), while article 1938 says that “hypothecs do not divest the debtor...of the hypothecated property”. Both hypothecs and privileges are charges (i.e. real rights for the purpose of providing security) over someone else's property. That is why section 121 of the Income Tax Act provides that the privilege for state taxes shall have “priority to all other privileged claims, charges or debts against such person”. “Charges” must include hypothecs and it would therefore make nonsense of section 74, which creates a priority *pari passu* with state taxes, to say that it gives no priority over hypothecated property because such property does not really belong to the debtor for the purposes of the section.

22. The Court of Appeal accepted these submissions by counsel on behalf of the Corporation and therefore rejected the extreme argument

that for the purposes of section 74, hypothecated property did not count as property of the debtor at all. But Rawlins JA accepted the argument in a modified form by holding that the effect of section 74 was to give the Corporation rights over property in which the bank, by reason of its hypothec, had a beneficial interest. The section therefore, he said, contravened the prohibition in section 6 of the Constitution on the compulsory taking of property other than for a public purpose and on payment of full compensation. On this ground, the appeal was allowed.

23. Their Lordships do not agree. At the time that the bank was granted its hypothec, section 74 (or its predecessor section 73 of the National Insurance Act 1978) was in force. The bank never obtained any rights over the company's property which was not subject to the priority accorded by statute to any claims for contributions which might exist when the bank's security came to be enforced. It follows that section 74 did not deprive the bank of any property and section 6 of the Constitution has no application.

24. Their Lordships will therefore humbly advise Her Majesty that the appeal should be allowed with costs and the judgment of Master Cottle restored.