IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

I TE KŌTI MATUA O AOTEAROA
TĀMAKI MAKAURAU ROHE

CIV-2015-404-002280
[2018] NZHC 453

BETWEEN	DEBUT HOMES LIMITED (IN LIQUIDATION) First Plaintiff
	HENRY DAVID LEVIN AND VIVIEN JUDITH MADSEN-RIES AS LIQUIDATORS OF DEBUT HOMES LIMITED (IN LIQUIDATION) Second Plaintiffs
AND	LEONARD WAYNE COOPER First Defendant
	LEONARD WAYNE COOPER AND TRACEY COOPER AS TRUSTEES OF THE L & T COOPER FAMILY TRUST Second Defendants

Hearing:	13-17 March, 9 October and 13 October 2017
Appearances:	P Shackleton and J Angelson for the First and Second Plaintiffs R Hucker, H Holland (March only) and R Selby (October only) for the First and Second Defendants
Judgment:	15 March 2018

JUDGMENT OF HINTON J

This judgment was delivered by me on 15 March 2018 at 3.00 pm pursuant to Rule 11.5 of the High Court Rules

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Registrar/Deputy Registrar

Solicitors:

Meredith Connell, Auckland
Hucker & Associates, Auckland

[1] The liquidators of the plaintiff company (Debut) are suing its sole director for breaches of the Companies Act 1993 (the Act).

[2] In particular, the liquidators say that the director incurred debts without a reasonable belief that Debut would be able to meet them when they fell due, in breach of s 136 of the Act. They plead related breaches of other duties.

[3] Unsecured creditor claims in the liquidation total $499,507. The bulk of this is GST debt owed to the Inland Revenue Department (the IRD), $366,011 core GST and $84,088 accrued interest and penalties. The balance is trade creditors. Mr Cooper and his ex-wife, Ms Cooper are owed about $210,000 on their shareholders' current account, but have not proven in the liquidation.

[4] The liquidators claim the full amount of $499,507 against the director.

Background

[5] Debut was a small business, which developed residential houses in New Plymouth. It was incorporated in 2005. Mr Cooper was the sole director and he worked full-time in the business. The shareholders were Mr and Ms Cooper.

[6] Up until 31 October 2012, Debut paid all of its debts when they fell due, including GST. It had completed a number of developments and had a number still on foot, funded by BNZ and JTJ (a second-tier lender). The loans from JTJ and BNZ were secured by mortgages and guaranteed by Mr Cooper.

[7] It is undisputed that Debut had been balance sheet insolvent from at least March 2009, but it was supported by the shareholder loans from the Coopers.

[8] In early September 2012, Debut entered into agreements to sell completed properties at 2 and 7 Karika Place for $586,000 and $240,000 respectively, including

GST. GST was not due until 30 November 2012.[1] The settlements took place in early to mid-October 2012. From the 2 Karika Place proceeds, Debut paid JTJ $490,390 and retained $93,600. From the 7 Karika Place proceeds, Debut paid JTJ $210,390 and retained $28,000.

[9] Debut was experiencing costs overruns and increasing debt. On 23 October 2012, JTJ emailed Mr Cooper confirming earlier advice that no further advances would be made to complete development projects. Mr Cooper met with Mr Furlong, Debut's accountant, twice in October to discuss Debut's funding requirements and performance.

[10] Mr Cooper said in evidence that by the end of October 2012, things were going sufficiently wrong that he considered he should look at folding the business. He did not have any confidence he could trade out.

[11] Mr Cooper prepared costings for Mr Furlong, and they met on 6 November 2012. The costings were put together, inter alia to try to get more funding from JTJ. The figures showed a surplus of $170,000. The costings included forecast further expenditure and estimated sale prices of the existing property stock, but made no provision for payment of GST by Debut, including GST on the September sales of 2 and 7 Karika Place, which was due on 30 November 2012. There was also no allowance for interest charges. The estimated sale prices were based on real estate agents' advice.

[12] I accept Mr Cooper's evidence that the costings were prepared in the form they were, at Mr Furlong's instruction.

[13] Mr Furlong's evidence is that at the meeting on 6 November 2012 he told Mr Cooper that the GST deficit would be $300,000 plus. Mr Cooper denies this evidence. I accept that Mr Furlong did give that advice. He referred to that figure in a letter dated 28 November 2013 to the New Zealand Institute of Chartered

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[1] This was obviously not a simple matter of GST on the sale price, as the company had GST credits, but at all relevant points the GST on sales was the predominant part of a return.

Accountants (NZICA) following a complaint by Mr Cooper. That was only one year after the 6 November 2012 meeting. In Mr Cooper's reply to Mr Furlong's letter, dated 10 February 2014, he says: "the GST shortfall was discussed".[2] Mr Cooper's letter is otherwise very thorough and I have no doubt he would have taken issue over the figure of $300,000 had that not been roughly correct.

[14] In any event, I consider little turns on the discussion of the GST deficit. Mr Cooper confirmed, as he had to, that he knew there was a GST liability on the sales and that he could figure out the amount. He would also have had a good handle on the GST inputs. He acknowledged that within reason he was perfectly capable of calculating what the deficit was going to be. The quantum of the GST liability and the likely deficit would have been reasonably clear to someone who had traded as a property developer for a number of years, and especially when that person is also an astute and careful business person, which Mr Cooper impressed me as being.

[15] As at early November 2012, Debut had six remaining properties. 48 and 27a Penrod Drive were already complete and rented out. 4 Karika Place was very close to completion. A house at 28 Coby Sydney Drive (the land about to be subdivided into two titles), and a house at 78 Pemberton Road, were at early stages of construction.

[16] After the 6 November 2012 meeting with Mr Furlong, Mr Cooper decided to limit trading to completing the partially-developed properties and to selling all properties as soon as possible.

[17] On 7 November 2012, Debut obtained further borrowing from JTJ with Mr Furlong's assistance, on the basis that Ms Cooper gave security over a $200,000 deposit she had with JTJ. (Mr Furlong was a shareholder in JTJ and also its accounting adviser.)

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[2] Initially Mr Cooper's letter to NZICA was not in evidence. However, after I allowed the defendants to belatedly raise an affirmative defence under s 138 of the Act, reserving leave to the plaintiffs to call further evidence, Mr Hucker (ultimately) did not object to the admission of Mr Cooper's letter to NZICA and I allowed it into evidence. (The defendants' position is recorded in a memorandum dated 20 June 2017.)

[18] On 9 November 2012, Debut sold 4 Karika Place for $589,000, including GST of $76,820. The full proceeds of sale were paid to JTJ by 7 December 2012.

[19] On 20 November 2012, Debut sold 48 Penrod Drive for $408,000 including GST, settling on 23 January 2013. $82,000 was retained by Debut and the balance paid to BNZ, the mortgagee of that property.

[20] As noted, GST on the two earlier Karika sales (numbers 2 and 7) was due for payment on 30 November 2012. It was not paid. From that date on, no GST payments were made by Debut.

[21] On 5 February 2013, 27a Penrod Drive was sold for $317,000, including GST of $41,000, settling on 8 March 2013. $272,000 was paid to BNZ as mortgagee and the balance of $44,000 retained.

[22] On 20 February 2013, Mr and Ms Cooper as trustees of the L and T Cooper Trust (the Trust) agreed to lend up to $380,000 to Debut as working capital. Mr and Ms Cooper were the settlors and primary beneficiaries of the Trust. Mr Cooper accepted that, to all intents and purposes, the Trust was "just himself and Ms Cooper". Minutes and a general security agreement (GSA) were signed in February/March 2013. Advances of $376,000 approximately were made by the Trust between March 2013 and February 2014.

[23] Mr Cooper's evidence was that, before the Trust started to make its advances in March 2013, Ms Cooper's $200,000 deposit was returned to her and the security released.

[24] In April 2013, 78 Pemberton Road was sold for $825,000 including GST, with settlement on 12 April 2013. The full proceeds were paid to JTJ.

[25] In May/June 2013, almost all of the residual JTJ debt was refinanced through the BNZ, the Trust agreeing to guarantee the BNZ debt of about $435,000, in addition to the existing guarantee of Mr Cooper.

[26] On about 13 September 2013, the IRD served a statutory demand and after that issued a liquidation proceeding. In mid-November 2013, after the demand had expired, a proposal was put to IRD and rejected.

[27] On 12 November 2013, 28C Coby Sydney Drive sold for $140,000, including GST of $18,000. The sale settled on 20 December 2013. $17,400 was paid to the Trust and the balance to BNZ.

[28] On 28 January 2014, 28b Coby Sydney Drive sold for $485,000, settling on 28 February 2014. $147,000 went to the Trust and $320,000 to the BNZ.

[29] On 7 March 2014, Debut went into liquidation on the IRD's application.

[30] In addition to the unsecured creditor claims of $499,507, Mr and Ms Cooper were still owed a current account debt of approximately $210,000 and over $200,000 of the $376,000 Trust loan was outstanding.

[31] For a period of approximately 18 months leading up to completion of the development work on the properties, Mr Cooper worked full-time for Debut and received no salary.

Breach of directors' duties

[32] The liquidators argue that Mr Cooper has breached ss 131, 135 and 136 of the Act and that compensation is payable under s 301.

Section 136

[33] I begin by considering s 136, on which the liquidators placed most emphasis and which I consider to be most directly relevant. That section provides:

> **136 Duty in relation to obligations**
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> A director of a company must not agree to the company incurring an obligation unless the director believes at that time on reasonable grounds that the company will be able to perform the obligation when it is required to do so.

[34] The liquidators say that in respect of each of the sale and purchase agreements from 2 and 7 Karika Place in early September 2012 onwards, GST having been incurred and not paid, Mr Cooper was in breach of s 136.

[35] As a preliminary point, I note that GST output tax is "incurred" in terms of s 136, on the signing of a sale agreement, and is payable on whatever date the GST return is due.[3] Mr Hucker argued at one point that the GST is not incurred until payment is due.

[36] I find that there was no breach of s 136 in connection with the GST obligations incurred in early September 2012, that is in relation to the sales of 2 and 7 Karika Place. The liquidators have the burden on the balance of probabilities of persuading me that there was such a breach and I am not satisfied that Mr Cooper had no reasonable belief that those obligations could be met when they were incurred in early September 2012. Even the liquidators accept that Debut was not clearly insolvent in a cash flow sense until the end of October 2012. It was not until the meeting between Mr Cooper and his accountant, Mr Furlong, in early November 2012 that there is clear evidence that Debut was unlikely to be able to pay its accounts as they fell due. Mr Cooper was very concerned over building issues and costs overruns, and loans were increasing, but there is insufficient evidence that persuades me as to a lack of reasonable belief on Mr Cooper's part, prior to the end of October 2012. Debut was insolvent in a balance sheet sense, but it had been for some years, and it seems the company had nonetheless paid any undisputed debt down to the date of the early November 2012 meeting, and in fact down to the end of November 2012, when it first defaulted on its GST obligations. Mr Cooper had not put the GST to one side, but he had no obligation to do so and the company had traditionally not done so, using the money for cashflow purposes.

[37] I find with regard to GST and other debts incurred after the end of October 2012 that Mr Cooper was in breach of s 136 of the Act. The costings Mr Cooper drew up at Mr Furlong's request for the meeting in early November 2012, made no provision for GST and showed an estimated surplus of $170,000, which Mr

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[3] See for example *Peace and Glory Society Ltd (in liq) v Samsa* [2009] NZCA 396 at [74].

Cooper and Mr Furlong knew would turn into a likely deficit of at least $130,000. The GST debt that had already accrued by 6 November 2012 on 2 and 7 Karika Place was about $104,000. While there would be some offset for GST on expenditure, Mr Cooper accepted that would come nowhere near the GST debt. The costings also made no provision for finance costs or contingencies. JTJ's interest was running at about 13 per cent per annum.

[38] Mr Cooper could not reasonably have believed when signing sale and purchase agreements and incurring GST obligations post 6 November 2012 that Debut would be able to meet GST debts when they fell due. Mr Cooper expressly accepted that when he entered into the sale agreement for 4 Karika Place (on 9 November 2012), he had no reasonable basis to believe "he" (obviously meaning Debut) would be able to pay the GST when it became due, and the same for 48 Penrod Drive.

[39] In fact, it seems there was a strategy put in place by Mr Cooper and Mr Furlong for Debut to not pay GST on the due dates; to pay later out of any surplus and negotiate with the IRD over the balance. Further, there was no material improvement in Debut's position after the 6 November 2012 meeting, which might have led to a change in reasonable belief. Mr Hucker submitted that the sale of 4 Karika Place was more profitable than expected, but as Mr Shackleton pointed out, overall the trading performance was worse than Mr Cooper's costings.

[40] I do not accept Mr Hucker's argument that non-payment flowed from secured creditors refusing to release funds for GST. There were at least some surplus proceeds that were not paid to the secured creditors, but not applied to GST. This applied, for example, on the sale of the Penrod Drive properties. A different policy was adopted on the sale of 4 Karika Place where JTJ received the full net proceeds, but notably without dispute or any apparent contrary effort from Debut. Payments were made to the Trust from settlement proceeds, clearly a matter of Mr Cooper's choice, rather than to the IRD. There was no attempt to make arrangements for any GST payment after the 6 November 2012 meeting, whether via secured creditors or with the IRD. As I say, there seems to have been a strategy put in place for the IRD to carry the risk of the true projected shortfall, and that is what happened.

[41] The points that Mr Hucker raises in defence of the claim under s 136, like the points raised on behalf of the director in *Peace and Glory Society Ltd*,[4] might be relevant under s 301 of the Act, but do not counter the breach of duty. These include matters such as Mr Cooper's having allegedly maximised return to Debut overall; the loss of his and his ex-wife's shareholder advances of $210,000 and the Trust's loss of $200,000 of its loan.

[42] My finding under s 136 with regard to the GST obligations, applies equally to other debts included in the total claim, all of which I understand were incurred after 31 October 2012.[5]

Sections 131 and 135

[43] For similar reasons, I also consider Mr Cooper was in breach of ss 131(1) and 135(b) of the Act after 31 October 2012.

[44] Section 131(1) provides:

> **131 Duty of directors to act in good faith and in best interests of company**
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> (1) Subject to this section, a director of a company, when exercising powers or performing duties, must act in good faith and in what the director believes to be the best interests of the company.
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> …

[45] Good faith requires the director to act bona fide, that is, the director must act honestly and with a proper motive when making decisions for the company. Acting in the company's best interests requires a director to consider what the best interests of the company actually are, and to act loyally in accordance with those interests. It requires the director to put the company's interests ahead of their own interests.

[46] In times of insolvency or near-insolvency, the duty to act in the best interests of the company will also require a director to consider the position of creditors.[6] If a

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4 *Peace and Glory Society Ltd (in liq) v Samsa* [2009] NZCA 396.

5 The caselaw tends to suggest that s 136 is best suited to single transactions, but I see no reason why it should not apply to the debts generally in a case like the present.

6 *Sojourner v Robb* [2006] 3 NZLR 808 (HC) at [102].

director fails to consider the obligations owed to creditors they cannot be said to be acting in good faith. Nor can a director be taken to be acting in the best interests of the company by failing to discharge obligations to creditors before promoting the interests of shareholders.

[47] Debut was balance sheet insolvent from incorporation and was unable to pay its due debts from 31 October 2012.[7] As such any decisions made by Mr Cooper should have given consideration to the obligations Debut owed to its creditors.

[48] Mr Cooper had personally guaranteed all of Debut's loans. Later, Ms Cooper had given JTJ a security over a $200,000 deposit for further lending. That was replaced by the trustees of the Trust giving a guarantee to BNZ which put the family home at risk. Mr Cooper, Ms Cooper and the Trust all had "skin in the game" and stood to suffer financial loss upon liquidation of Debut.

[49] Mr Cooper's personal interests and those of his wife and the Trust were in direct conflict with the best interests of Debut and his duty as director to promote those interests. Mr Cooper acted in his own interests when he sought to pay off the secured and guaranteed debts. In doing so he neglected to satisfy the obligation of Debut to account for GST to the Commissioner. The GST collected on the sales was instead used to pay off the guaranteed and secured debts and create cashflow which was applied to the completion of the other properties, the proceeds of which were used in similar fashion. The ultimate result was to reduce the guarantee liability of Mr Cooper and the Trust.

[50] Mr Cooper has breached his duty under s 131(1) in two regards. Mr Cooper neglected to satisfy the obligations of a creditor, the Commissioner, when he applied the funds realised from the sale of properties to fund further work and to satisfy secured debts for which he was personally liable by virtue of his guarantee. In doing so he was not acting in good faith as he was not considering the obligations that Debut owed to *all* its creditors. Secondly, Mr Cooper was acting in his own interests above those of Debut. By failing to pay GST to the Commissioner, Mr Cooper was creating a new debt for Debut, which would be subject to penalties and interest totalling

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7 Both experts gave evidence to this effect.

$84,088.31, while limiting his own liability for debts guaranteed by himself. No director of a company could seriously believe in good faith that accruing a large tax debt, with no way of paying it, could be in a company's best interests.

[51] Section 135(b) provides:

> **135 Reckless trading**
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> A director of a company must not—
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> …
>
> (b) cause or allow the business of the company to be carried on in a manner likely to create a substantial risk of serious loss to the company's creditors.

[52] The test is an objective one.[8] The Court in determining whether a breach of s 135 has occurred is not concerned with what the director actually believed, instead the focus is on the manner in which the company's business is carried on and whether that created a substantial risk of serious loss to the creditors.

[53] A gloss is often added to the term "substantial risk" such that it is read as differentiating between legitimate and illegitimate risks.[9] All businesses take risks and often these will be substantial, albeit legitimate. However, when a business finds itself in troubled financial waters, directors need to raise their level of vigilance and take a sober assessment of the company's future prospects.[10] When prospects are grim, it will rarely be reasonable for a company to be carried on in a way which creates a risk of loss to its creditors.

[54] There can be no doubt that Mr Cooper has "caused the business of the company to be carried on". He was the sole director and solely responsible for its management. Any decisions made and the outcomes of those decisions can be causatively linked to him.

[55] The risk created by Mr Cooper to the Commissioner in the form of unpaid GST was more than substantial. By early November 2012, Mr Cooper was aware that

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8 *Mason v Lewis* [2006] 3 NZLR 225 (CA) at [50].
9 *Mason v Lewis* at [49].
10 *Mason v Lewis* at [48] and [51].

Debut was facing a pending GST deficit in the realm of $300,000 and it would at best wind up with $170,000 to meet that deficit. The way Mr Cooper carried on the business, neglecting to pay GST, and putting those funds towards the satisfaction of debts which he and the Trust had guaranteed, meant that loss to the Commissioner was inevitable.

[56] Moreover, the loss to the Commissioner was undeniably serious. The GST debt owed, following the final sale, was $366,011. The Commissioner stood to lose the entirety of this amount, with no hope of recovery without instituting liquidation proceedings.

Affirmative defence under s 138 – reliance on professional advice

[57] Mr Cooper claims, under s 138 of the Act, to have a defence against findings that he breached the foregoing duties to Debut. The relevant parts are:

> **138 Use of information and advice**
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> (1) Subject to subsection (2), a director of a company, when exercising powers or performing duties as a director, may rely on reports, statements, and financial data and other information prepared or supplied, and on professional or expert advice given, by any of the following persons:
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> …
>
> (b) a professional adviser or expert in relation to matters which the director believes on reasonable grounds to be within the person's professional or expert competence:
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> …
>
> (2) Subsection (1) applies to a director only if the director—
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> (a) acts in good faith; and
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> (b) makes proper inquiry where the need for inquiry is indicated by the circumstances; and
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> (c) has no knowledge that such reliance is unwarranted.

[58] How s 138 operates as a "defence" is unclear. I agree with the plaintiffs' argument that the section is arguably superfluous,[11] because if it was reasonable to rely

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[11] The plaintiffs rely inter alia on Peter Watts *Director's Powers and Duties* (2nd ed, LexisNexis, Wellington, 2009) at 239.

on professional advice, that will go against a breach of duty in any event. Consistent with those observations, there do not seem to be any cases where a director has successfully relied on s 138.

[59] Mr Cooper's defence under this section is premised on advice which he says was given to him by Mr Furlong at or around the meeting of 6 November 2012, including that Mr Furlong encouraged him not to shut down the company; told him Debut could trade out of its difficulties and it would be okay. Mr Cooper says Mr Furlong never pointed out the IRD deficit of $300,000 and that he said GST could be used for cashflow and either paid later or negotiated later with the IRD.

[60] The statements relied on are very vague and, consistent with that vagueness, somewhat shifting between Mr Cooper's evidence and his counsel's submissions.

[61] I have already found that the GST deficit was discussed at the meeting and that in any event Mr Cooper knew of it.

[62] The view I have formed of the November 2012 meeting is based in particular on the NZICA correspondence, my clear impression of which was not altered by hearing from Mr Furlong and Mr Cooper. It seems that they discussed Debut's likely shortfall and Mr Furlong said that JTJ would pursue Mr Cooper to bankruptcy, whereas he considered the IRD would negotiate and be likely to write off any shortfall. Mr Cooper then decided that the IRD would be the lesser of the two evils. Coupled with that, I accept that Mr Furlong probably did use language such as that Debut should be okay, or should be able to trade out.

[63] However, none of this is advice of the sort contemplated by s 138. It is not advice Mr Cooper relied on "when performing duties", which is a predicator to s 138. Rather, it is advice on how to deal with the consequence of failing to perform duties. It is too vague to fall into the category of professional or expert advice for purposes of s 138, and it would clearly require "proper inquiry" for the same reasons I have referred to already. Not only did Mr Cooper not make proper inquiry, he must have known Mr Furlong's advice was at best wishful thinking. A director would also not be acting in good faith to rely on such generalised and loose statements.

[64] In particular, Mr Cooper would not be acting in good faith in relying on Mr Furlong saying Debut would be okay or could trade out, given the clear substantial projected shortfall of which I have already found he was either told by Mr Furlong, or could quite readily calculate himself.

[65] Further, I cannot even accept that there was a plan to trade out of difficulties in any meaningful sense, when the IRD was ignored and such a large debt allowed to accumulate. Mr Cooper says he understood Mr Furlong had been in touch with the IRD but that is implausible. There would have been evidence of Mr Cooper at least seeking reassurance from Mr Furlong on that front. Instead, there was complete silence vis-à-vis the IRD until it followed up, and no effort post 6 November 2012 to run any further numbers, on the part of Mr Cooper or Mr Furlong. The accumulation of a $366,000 debt to the IRD is consistent with only one course. Mr Cooper (and Mr Furlong) had decided to sell off all the assets and see what, if anything, could be sorted with the IRD at the end of the day. As he acknowledged in his letter to NZICA, Mr Cooper considered that dealing with the IRD was the lesser of two evils. That is not implementation of a plan to "trade out" or reliance on things being "okay".

[66] Section 138 of the Companies Act therefore does not apply and I find against Mr Cooper on his affirmative defence.

[67] I should add that I accept Mr Furlong's advice appears to have been unsatisfactory, but for good reason it does not operate as a defence.

Compensation under s 301 for breach of duty

[68] The compensation payable for breach of duty under ss 131, 135 and 136 is covered by s 301 of the Act.

[69] Under s 301, the Court can order a director who is in breach of duty to a company, to contribute such sum to the assets of the company by way of compensation as the Court thinks just.

[70] The relevant parts of the section are:

301 Power of court to require persons to repay money or return property

(1) If, in the course of the liquidation of a company, it appears to the court that a person who has taken part in the formation or promotion of the company, or a past or present director, manager, administrator, liquidator, or receiver of the company, has misapplied, or retained, or become liable or accountable for, money or property of the company, or been guilty of negligence, default, or breach of duty or trust in relation to the company, the court may, on the application of the liquidator or a creditor or shareholder,—

(a) inquire into the conduct of the promoter, director, manager, administrator, liquidator, or receiver; and

(b) order that person—

(i) to repay or restore the money or property or any part of it with interest at a rate the court thinks just; or

(ii) to contribute such sum to the assets of the company by way of compensation as the court thinks just; or

…

[71] The liquidators seek an order for payment of $499,507, being the total of the creditor claims filed in the liquidation.

[72] The liquidators rely on *Sojourner v Robb*,[12] saying that the present case similarly involved a breach of s 131, with consequent fiduciary obligations. *Sojourner v Robb* was a case where the directors sold tangible assets to a new company, without bringing goodwill to account. Liquidation followed, leaving unsecured creditors with nothing. As the Court said, it was analogous to a breach of trust and the appropriate relief, rather than being compensatory, was restitutionary, in the form of an account of profits generated by the new company's business.[13]

[73] There are a number of different ways of assessing compensation, as the Court of Appeal noted in *Lower v Traveller*.[14]

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12 *Sojourner v Robb* [2007] NZCA 493, [2008] 1 NZLR 751.
13 At [53].
14 *Lower v Traveller* [2005] 3 NZLR 479 (CA).

[74] Lang J in *Goatlands Ltd (in liq) v Borrell*[15] referred to the approach argued for by the liquidators, of the director being ordered to make good all the losses suffered by creditors, as applying in "extreme cases". He said as follows:

> [119] Sections 320(1) and 321(1) of the 1955 Act vested similar powers in the Court to require directors who had been found to have breached their duties under the Act to pay compensation, or take responsibility for the debts of the company, to such extent as the Court thought just. As the Court of Appeal noted in *Lower v Traveller* (at [78]), s 320 of the 1955 Act "conferred a power on the Court in the exercise of its judgment, if it thought proper to do so, to impose personal liability without limitation on an impugned officer of a company for all or any part of its debts". The Court also said that the principal purpose of the section was to compensate those who suffered loss as a result of illegitimate trading.
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> [120] In extreme cases, such as *Wait*, the Court might order the directors in default to make good all of the losses suffered by creditors. More often, however, the Court would require the directors to make good any losses that creditors had suffered during the period in which the directors had permitted the company to trade whilst insolvent. An example of this approach is in *Lower v Traveller* in which the Court of Appeal upheld (at [80]) the decision of William Young J at first instance requiring the directors of the company to make good the losses caused by illegitimate trading from a specified date.

[75] In *Re Wait Investments*, the company, with capital of $100, was managed by an officer with personal debts amounting to $17 million, who was operating under an insolvency proposal. With no pre-existing finance in place, the company entered into an unconditional purchase agreement for a property worth $1.635 million.[16] The company was subsequently unable to obtain finance, failed to settle and the vendor resold at a loss. Barker J held that a prudent director or manager, given the circumstances, would have considered that there was a real possibility that finance for the purchase of the property would not be obtainable.[17] His Honour held that the errant director or manager must be liable for the full loss, since he had abused the protection of limited liability and would have been fully liable had he entered into the agreement personally.[18] The other director of the company, was held less culpable, but still

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15 *Goatlands Ltd (in liq) v Borrell* (2007) 23 NZTC 21,107 (HC).
16 *Re Wait Investments Ltd (In Liquidation)* [1997] 3 NZLR 96 (HC).
17 At 103.
18 At 105.

ordered to pay half the total loss,[19] the result being that an amount greater than the total loss was awarded against the directors.

[76] I do not consider the present case to be one of the more extreme cases of director misconduct.

[77] While undoubtedly Mr Cooper was acting overall in significant preference to "his" own creditor position, he (through the Trust) nonetheless injected significant new funds in the course of the ongoing work, and lost those funds in material part. He worked for one-and-a-half years without pay. Mr Cooper had always paid all creditors down to November 2012 and he says, even at the end, close to half of the relatively small quantum of unsecured creditors, aside from the IRD, was disputed.

[78] While Mr Cooper was clearly in breach and was clearly preferring secured creditors and therefore himself, he mistakenly viewed his actions as being the best likely outcome for all creditors, including the IRD, because he understood that the only parties who would receive funds on a liquidation would be the secured creditors. He did not appreciate that on a liquidation or on a mortgagee sale, the IRD becomes a preferential creditor. He saw himself as, if anything, improving the position of unsecured trade creditors by completing buildings rather than leaving those creditors in the lurch. My understanding is that the total unsecured creditors other than the IRD would have been materially worse in a 31 October 2012 liquidation, than in the actual liquidation.

[79] I consider this present case falls more into the general category of cases referred to by Lang J, where the Court approaches compensation from the starting point of debts incurred (and not paid) between the breach date and the date of liquidation.

[80] Whichever basic approach a Court might take, other factors may still affect the answer, particularly questions of causation, culpability and duration of trading. So, for example, in *Peace and Glory Society Ltd*, the IRD had encouraged Mr Samsa to

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[19] At 105.

sell a property when the company was insolvent.[20] He sold it to another entity he owned, but not at an undervalue, and all the proceeds went to secured creditors, leaving the IRD unpaid for GST. Had the sale been by liquidators or the mortgagee, GST would have been a preferential debt and been paid in priority to the mortgage.[21] The liquidators brought a claim under s 136, which the Court found was breached by the sale, but it exercised its discretion against compensation because in effect Mr Samsa had not directly caused the loss.[22]

[81] In *Traveller v Lower* Young J awarded $8.4 million out of a total shortfall of about $40 million in circumstances where he concluded the company should have ceased trading by April 1994, instead of which it embarked on an extraordinary programme of expansion and continued to trade for about three years.[23] Mr Lower had obtained substantial benefits and was found to have a level of culpability near to the most serious of illegitimate trading. Still substantial deductions were made. A related party debt of $17.271 million, which was to be subordinated, was set aside. A $9.2 million allowance was made for losses the creditors would have suffered in any event, had the company been placed into liquidation at the date of breach. A reduction of $6 million was granted for uncertainties in the calculation, and a final reduction of approximately $3 million was granted for risks which creditors would have factored into the prices of their goods and services.

[82] In *Goatlands*, Lang J ultimately awarded one quarter of what was essentially a GST debt, being the percentage by which he considered the risk in using a GST refund following purchase was illegitimate when the purchase was subsequently cancelled and the GST had to be repaid, but the funds were not available.[24] The funds had been used on the property that was lost, and not diverted elsewhere.

[83] I have decided to approach the measure of compensation from what seems to be the more general starting point of the debts incurred between the breach date of 31 October 2012 and the date of liquidation. Assuming all of the unsecured debts were

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20 *Peace and Glory Society Ltd (in liq) v Samsa* [2009] NZCA 396.
21 At [74].
22 At [76].
23 *Re South Pacific Shipping Ltd (in liq); Traveller v Lower* (2004) 9 NZCLC 263,570 (HC).
24 *Goatlands Ltd (in liq) v Borrell* (2007) 23 NZTC 21,107 (HC) at [134].

incurred after 31 October 2012, except for the GST debt on the sales of 2 and 7 Karika Place, and deducting $100,000 for that debt, the resulting figure (excluding IRD interest and penalties) is $316,000 approximately.

[84] I consider it relevant for purposes of s 301 that Mr Cooper worked for no salary for 18 months to complete the properties and the Trust lent funds, which were new monies, to facilitate completion of the properties. While partly repaid, the Trust was left with a deficit of $200,000. Mr Cooper's work and the injection of the Trust funds enabled significantly higher sale prices and therefore a significantly higher GST debt. The total input from Mr Cooper and the Trust would have had a value of at least $320,000 and more relevantly, probably close to doubled the total GST debt on the sales post 2 and 7 Karika Place.

[85] I make an allowance to Mr Cooper of $80,000 as a small recognition of the post 31 October 2012 input from himself and the Trust. The allowance has to be much less than Mr Cooper's input, and much less than the increase in core GST, to recognise that his actions were in breach of duty.

[86] As the figure finally taken into account in respect of IRD debt is therefore approximately half the core debt, I add half of the claimed accrued interest and penalties, to reach a rounded compensation figure of $280,000. I note in terms of IRD interest and penalties that the Court of Appeal, in an obiter statement in *Peace & Glory*,[25] suggested these were not recoverable under s 301. I would not have thought that correct. The section has a wider ambit than that. Mr Hucker raised no argument to the contrary.

Voidable preferences

[87] The liquidator's next cause of action contends that certain payments made by Debut to Mr Cooper can be declared voidable, and therefore recovered by Debut, under s 292(1) of the Companies Act 1993. The relevant parts are:

> **292 Insolvent transaction voidable**

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[25] *Peace and Glory Society Ltd (in liq) v Samsa* [2009] NZCA 396.

(1) A transaction by a company is voidable by the liquidator if it—

(a) is an insolvent transaction; and

(b) is entered into within the specified period.

(2) An **insolvent transaction** is a transaction by a company that—

(a) is entered into at a time when the company is unable to pay its due debts; and

(b) enables another person to receive more towards satisfaction of a debt owed by the company than the person would receive, or would be likely to receive, in the company's liquidation.

(3) In this section, **transaction** means any of the following steps by the company:

…

(e) paying money (including paying money in accordance with a judgment or an order of a court):

…

(4B) Where—

(a) a transaction is, for commercial purposes, an integral part of a continuing business relationship (for example, a running account) between a company and a creditor of the company (including a relationship to which other persons are parties); and

(b) in the course of the relationship, the level of the company's net indebtedness to the creditor is increased and reduced from time to time as the result of a series of transactions forming part of the relationship;

then—

(c) subsection (1) applies in relation to all the transactions forming part of the relationship as if they together constituted a single transaction; and

(d) the transaction referred to in paragraph (a) may only be taken to be an insolvent transaction voidable by the liquidator if the effect of applying subsection (1) in accordance with paragraph (c) is that the single transaction referred to in paragraph (c) is taken to be an insolvent transaction voidable by the liquidator.

(5) For the purposes of subsections (1) and (4B), **specified period** means—

(a) the period of 2 years before the date of commencement of the liquidation together with the period commencing on that date and ending at the time at which the liquidator is appointed; and

…

[88] The purpose of the voidable transaction power is to ensure that fairness is achieved between creditors. Where one creditor has been unduly preferred, to the detriment of the other creditors, s 292(1) allows a liquidator to reach back in time and set aside transactions which occurred while a company was insolvent, but not yet in liquidation. The result is that there is a larger pool of funds or assets from which the creditors may claim.

[89] The liquidators contend, and I accept their evidence, that from 31 October 2012 until the date of liquidation on 7 March 2014, payments were made by Debut to Mr Cooper totalling $35,918. The payments involved cash withdrawals through ATMs and transfers of funds to Mr Cooper's personal account, all from Debut's account. These payments had the effect of reducing the liability of Debut to Mr Cooper as an unsecured creditor.

[90] I also accept the evidence of Mr Cooper, which the liquidators similarly accepted in closing, that payments amounting to $1,788.46 relating to spending on supermarkets and hospitality, were for company purposes, although recorded as drawings. That brings the total amount which the liquidators seek to have declared voidable to $34,129.54.

[91] Mr Cooper gave evidence to the effect that repayments made by himself in the relevant period to March 2014, totalling $11,528.58, should have been taken into account by the liquidators in arriving at their sum. Any repayments made by Mr Cooper in this period can only be taken into account in determining whether a running account existed between himself, as a creditor, and Debut for the purposes of s 292(4B). The effect of such a finding would be that all the transactions which took place between Debut and Mr Cooper as creditor, would be treated as a single transaction in determining whether Mr Cooper received more towards satisfaction of his debt than he would have in Debut's liquidation.

[92] I find that no running account existed. Nothing suggests to me that the payments were made to Mr Cooper with "the predominant purpose of inducing the

provision of further supply". A cash payment to Mr Cooper by Debut cannot be considered as inducing the provision of further supply by Mr Cooper back to Debut in the form of a smaller sum of money.

[93] In order for the payments to Mr Cooper by Debut to be voidable by the liquidators the Court must be satisfied that:

(a) there is a transaction which falls within the categories listed in s 292(3); and

(b) the transaction occurred within the specified period; and

(c) the transaction was entered into at a time when the company was unable to pay its due debts; and

(d) the transaction enabled the creditor to receive more towards satisfaction of a debt owed by the company than the person would receive, or be likely to receive, in the company's liquidation.

[94] I am satisfied that the above are all made out. The transaction involved payment of money to Mr Cooper. The transaction also occurred within the specified period, being two years prior to the application by Inland Revenue to the High Court for Debut to be liquidated on 31 October 2013, and including the period leading up to the making of the order on 7 March 2014.

[95] The transactions were also entered into at a time when Debut was unable to pay its due debts. I accept the evidence of the liquidators that Debut did not have the necessary cashflow to pay its due debts from 31 October 2012. I note that the evidence of Mr McKay, the expert witness for Mr Cooper, was also that Debut was unable to pay its due debts from around this period in time.

[96] Mr Cooper undoubtedly received more towards satisfaction of his own unsecured debt owed by Debut than he would have received had he proved his claim to the liquidators and lined up alongside the Commissioner. As matters stand, had Mr Cooper proved his claim he would have stood to receive nothing. The evidence

suggests that there are insufficient assets in Debut's liquidated estate to meet existing preferential claims. Therefore, I am satisfied that the final requirement of s 292 is satisfied.

[97] Mr Cooper argues that the unpaid hours he put into completing the properties would not have been undertaken by him had he known that the drawings he took were voidable. That no doubt is true, but it is not a defence to a claim under s 292(1), the requirements of which have been met. The relevant amounts paid were not salary for services performed, they were drawings against Debut's indebtedness to Mr Cooper. Unfortunately for Mr Cooper, they cannot be reclassified, except to the extent I have already allowed. I note also that I have taken Mr Cooper's extensive unpaid work into account in assessing compensation under s 301.

Challenge to the Trust's secured debt

[98] Finally, the liquidators seek directions and orders concerning how the sum recovered from Mr Cooper is to be applied in satisfaction of creditor claims.

[99] At this point, the only significant creditor to have proved in the liquidation is the Commissioner. However, the Trust asserts that it still retains a GSA over all of Debut's present and after acquired property. The concern of the liquidators is that the Trust will seek to enforce the GSA against the liquidators following judgment, effectively depriving the Commissioner, as the only substantial unsecured creditor to have proved in the liquidation, of the fruits of the litigation.

[100] The liquidators argue, and I agree, that it is inherently wrong that an amount awarded to the liquidators for distribution to unsecured creditors who have proved their claim in the liquidation, can be indirectly returned to Mr Cooper through the enforcement of the Trust GSA.

[101] The liquidators advanced a number of causes of action directed towards a result that the Trust is not entitled to claim in the liquidation, at least against any award I make against Mr Cooper in his capacity as director.

[102] First, the liquidators contend that they gave notice in writing under s 305(8) of the Act, requiring the Trust to elect which of the options granted to it in 305(1)(a)-(c) it intends to rely on and the trustees failed to comply. They say the trustees must be taken as having surrendered their charge to the liquidators under s 305(9).

[103] The relevant subsections are:

> **305 Rights and duties of secured creditors**
>
> (1) A secured creditor may—
>
> (a) realise property subject to a charge, if entitled to do so; or
>
> (b) value the property subject to the charge and claim in the liquidation as an unsecured creditor for the balance due, if any; or
>
> (c) surrender the charge to the liquidator for the general benefit of creditors and claim in the liquidation as an unsecured creditor for the whole debt.
>
> …
>
> (8) The liquidator may at any time, by notice in writing, require a secured creditor, within 20 working days after receipt of the notice, to—
>
> (a) elect which of the powers referred to in subsection (1) the creditor wishes to exercise; and
>
> (b) if the creditor elects to exercise the power referred to in paragraph (b) or paragraph (c) of that subsection, exercise the power within that period.
>
> (9) A secured creditor on whom notice has been served under subsection (8) who fails to comply with the notice, is to be taken as having surrendered the charge to the liquidator under subsection (1)(c) for the general benefit of creditors, and may claim in the liquidation as an unsecured creditor for the whole debt.
>
> …

[104] The liquidators say they wrote to the trustees on 7 March 2014, requiring them to make an election pursuant to s 305(8) of the Act (the first notice). The notice, instead of being sent directly to the trustees, was sent to RMY Legal, who the liquidators believed were acting for the trustees. RMY Legal replied on 17 March 2014, informing the liquidators that they were no longer acting, but had forwarded the notice to Paul Gallagher Legal. Mr Cooper denied receipt of the notice.

[105] On 8 April 2014, the liquidators' first report, which contained a s 305 notice on the fourth page, was sent personally to Mr Cooper and Ms Cooper (the second notice). In cross-examination, Mr Cooper accepted that the report was delivered to his address.

[106] The liquidators contend that the first and/or second notice constituted a properly-served notice in terms of s 305.

[107] In determining whether there was effective notice, I must consider the provisions of the Act concerning service. In doing so I must ascertain the meaning of the enactment from its text and in light of its purpose.

[108] Section 391(1) of the Act sets out the requirements as to service upon creditors who are natural persons. The relevant parts are:

> **391 Service of documents on shareholders and creditors**
>
> (1) A notice, statement, report, accounts, or other document to be sent to a shareholder or creditor who is a natural person may be—
>
> (a) delivered to that person; or
>
> (b) posted to that person's address or delivered to a box at a document exchange which that person is using at the time; or
>
> (c) sent by facsimile machine to a telephone number used by that person for the transmission of documents by facsimile.
>
> …

[109] Section 392(1) contains additional provisions relating to service. It provides in relevant part:

> **392 Additional provisions relating to service**
>
> (1) Subject to subsection (2), for the purposes of sections 387 to 391,—
>
> (a) if a document is to be served by delivery to a natural person, service *must* be made—
>
> (i) by handing the document to the person; or
>
> (ii) if the person refuses to accept the document, by bringing it to the attention of, and leaving it in a place accessible to, the person:

> (b) a document posted or delivered to a document exchange is deemed to be received 5 working days, or any shorter period as the court may determine in a particular case, after it is posted or delivered:
>
> (c) a document sent by facsimile machine is deemed to have been received on the working day following the day on which it was sent:
>
> …

[110] The language of s 391 requires that the notice be actually delivered to the person, posted to that person's address, or sent by facsimile to a number used by that person for the transmission of documents by facsimile.

[111] The first notice was not sent to the Coopers personally, instead it was sent to the law firm that the liquidators assumed were acting for them. Had the notice been handed on by the law firm to Mr and Ms Cooper, that would seem to constitute service in terms of s 391(1)(a) and s 392(1)(a)(i).

[112] However, I am not satisfied that the first notice was in fact delivered, posted or faxed to Mr Cooper, via his lawyer, Paul Gallagher Legal. The liquidators have asked the Court to draw an inference that service was effected, on the basis that a request for discovery of the notice sent to Mr Gallagher was not responded to by Mr Cooper. They say that the defence ignored this request because to respond to it would prove service was effected. I am not prepared to draw such an inference. I am not satisfied that the first notice was properly served.

[113] I am also not prepared to find that the second notice constituted a notice in terms of s 305. While a s 305 notice may not have to be in distinct form, a notice to which a secured creditor does not respond has the effect of deeming a security interest to be surrendered. It is therefore important that what constitutes a notice is not read down. There is no obligation on a creditor to read, let alone open, a liquidator's report. If service could be effected by provision of a report which contained a notice (without more), secured creditors may inadvertently surrender their security interests, without having it fairly drawn to their attention that such interests were at threat. Mr Cooper, while accepting in cross-examination that he did in fact receive the liquidators' first report, was not asked whether he opened the report, nor whether he was aware that a

s 305 notice was contained within it. Nor did any evidence that he did give provide a sufficient basis for inferring that such was the case.

[114] Therefore, I find that the second notice did not constitute notice in terms of s 305 and the security interest was not surrendered.

[115] Though I am not prepared to find that the Trust surrendered its security interest by failing to comply with a s 305 notice, I agree with the liquidators that an order can be made setting aside the Trust's GSA under s 299 of the Act.

[116] The relevant parts are:

> **299 Court may set aside certain securities and charges**
>
> (1) Subject to subsection (2), if a company that is in liquidation is unable to meet all its debts, the court, on the application of the liquidator, may order that a security or charge, or part of it, created by the company over any of its property or undertaking in favour of—
>
> (a) a person who was, at the time the security or charge was created, a director of the company, or a nominee or relative of or a trustee for, or a trustee for a relative of, a director of the company; or
>
> (b) a person, or a relative of a person, who, at the time when the security or charge was created, had control of the company; or
>
> (c) another company that was, when the security or charge was created, controlled by a director of the company, or a nominee or relative of or a trustee for, or a trustee for a relative of, a director of the company; or
>
> (d) another company, that at the time when the security or charge was created, was a related company,—
>
> shall, so far as any security on the property or undertaking is conferred, be set aside as against the liquidator of the company, if the court considers that, having regard to the circumstances in which the security or charge was created, the conduct of the person, relative, company, or related company, as the case may be, in relation to the affairs of the company, and any other relevant circumstances, it is just and equitable to make the order.
>
> …

[117] For an order to set aside a security over company property to be made under s 299(1), a company must:

(a) be in liquidation; and

(b) unable to meet all its debts; and

(c) the security must have been created in favour of a related person (as described in the section).

[118] The Court must then consider the circumstances in which the security was created, the related person's conduct vis-à-vis the affairs of the company, any other relevant circumstances, and finally, whether it is just and equitable to make the order.

[119] As I held earlier, Debut is in liquidation and is unable to meet all its debts.

[120] The security was created in favour of Mr Cooper and Ms Cooper as settlors, trustees and principal beneficiaries of the Trust and they are both related persons as described, Mr Cooper being a director and Ms Cooper, his then wife.

[121] However, in considering the relevant circumstances surrounding the GSA and whether it is just and equitable to make such an order, I specifically note that much of the previous case law concerning s 299 is not analogous to the present case.

[122] In *Petterson v Browne,* the Court of Appeal allowed an appeal and overturned the High Court decision not to set aside a security granted in favour of the defendant.[26] The respondent, Mr Browne, organised for various unsecured loans advanced by himself and related third parties, to be repaid and replaced by a fresh advance from Mr Browne, which was secured by a general security agreement.[27] This was done at a time where the company was facing a financially disastrous claim for losses caused to a third-party company.[28] The Court found that the exchange of the unsecured loans for secured loans was done with a view to protecting the interests of the respondent and related third parties from the claim and set aside the security.[29]

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26 *Petterson v Browne* [2016] NZCA 189.
27 At [30].
28 At [28].
29 At [100].

[123] In *Harris v Bank of New Zealand,* Jagose J set aside a security granted in favour of the second respondent, The Bankhouse Trust Ltd, a company which shared a sole director with the company in liquidation.[30] Bankhouse had advanced over $1.28 million dollars, as unsecured lending, prior to 23 January 2014.[31] On 20 January 2014, a statutory demand was issued against the company.[32] Three days later the security was granted to Bankhouse, securing all its prior lending.[33] His Honour found that the security agreement conferred unfair advantage on Bankhouse over other creditors, particularly given that Mr Olliver was sole director of both companies, and set aside the security under s 299 of the Act[34]

[124] Common to those two cases is that previous unsecured lending, by a related third party, was granted a security at a time where the company faced financial peril. The Court of Appeal and High Court, in both cases, found that the purpose of granting the security was to protect the related third party from the financial fallout of liquidation. For that reason, it was just and equitable to set aside the security.

[125] Here, the GSA was granted on 22 March 2013. The Trust made advances to Debut totalling $376,816.56 over the period 4 March 2013 to 11 February 2014.[35] The great majority of those advances were not made as unsecured debt that was later granted a security, but as a secured loan from the outset. It can be presumed that such an advancement of funds, at a time when Debut was in a perilous financial position, would not have been made without the security being granted.

[126] I find some support in the obiter comments of Downs J in *Madsen-Ries v Greenhill* in reaching the view that this is nonetheless an appropriate instance in which to exercise the jurisdiction under s 299.[36]

[127] In *Madsen-Ries*, Mr Greenhill, the sole director of the company, had arranged for a debt he owed to the company to be reduced by $340,000 in exchange for a debt

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30 *Harris v Bank of New Zealand* [2017] NZHC 2374.
31 At [60].
32 At [60].
33 At [60].
34 At [61]-[62].
35 Debut subsequently repaid $146,770 to the Trust, leaving a balance in excess of $200,000 still owing.
36 *Madsen-Ries v Greenhill* [2016] NZHC 3188, [2017] NZCCLR 6 at [111]-[112].

the company owed to a trust, of which Mr Greenhill and his wife were trustees, being similarly reduced by the same amount.[37] The amount the company owed to the trust was secured by a general security agreement.[38] The amount outstanding after the write-off remained a substantial sum of over $575,000.[39]

[128] Mr Greenhill was found to have breached a number of duties in relation to the company. These included a breach of s 131 on account of promoting the director's own interests at the expense of the company, breach of s 135 for engaging in reckless trading after the company was insolvent, and a breach of s 136 by incurring GST and PAYE obligations to the Commissioner without a reasonable belief in being able to perform them as they fell due. Mr Greenhill was also held liable under s 346 of the Property Law Act 2007, for disposing of the property of the company, while the company was insolvent, with an intent to prejudice a creditor. Compensation awarded against him in favour of the company was $568,889.58.

[129] Though Downs J determined the security that the trust had over the company's property had been surrendered in accordance with s 305, he said (obiter) that had he not so found, he would have exercised jurisdiction under s 299 to set aside the security of the related third-party trust.[40] This was despite the fact that the trust had been granted the security at a time when the company was solvent and had advanced considerable funds to the company since then. Weighing in favour of setting aside was the fact that the trust was likely the alter-ego of Mr Greenhill and would not have authorised proceedings to be brought against Mr Greenhill in order to recover the outstanding debt.

[130] The GSA that the trustees hold over all the present and after-acquired property of Debut, was granted on 22 March 2013 and was registered on the Personal Property Securities Register on 9 April 2013.

[131] I have already accepted the evidence that Debut did not have the necessary cashflow to pay its due debts from 31 October 2012, almost five months prior to the

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37 At [15].
38 At [11].
39 At [15].
40 At [111].

GSA being granted. The natural inference is that while the Trust might not have advanced the money without a security, Debut in granting the security was protecting the interests of a related third party, at a time when it was clearly incapable of meeting its obligations to all its unsecured creditors.

[132] The trustees have not sought to claim in the liquidation. Had they done so, the liquidators could have made further claims for those losses. Given that the Trust, if not the alter-ego of Mr Cooper, is clearly a closely related third party, it is unlikely that it would authorise proceedings being brought against Mr Cooper personally. It would frustrate the purpose of the liquidators pursuing judgment against Mr Cooper as a director if Mr and Ms Cooper as trustees were able to claim the benefit of the judgment through the GSA and indirectly return it to Mr Cooper.

[133] The liquidators have suggested, and I agree, that the discretion to set aside the GSA, need not set it aside in its entirety. The Court is entitled to set aside the security only in part. I would adopt this course and set aside the GSA only against the amounts awarded to the liquidators in respect of compensation under s 301 and in respect of the voidable transaction under s 292. Therefore, if any other amounts later become available to satisfy the creditors of Debut, the Trust may invoke the GSA in respect of those amounts.

[134] For these reasons, I consider it just and equitable that the Trust GSA be set aside as against the amount awarded in this judgment.

[135] For present purposes, the Trust therefore becomes an unsecured creditor of Debut and may only share in the distribution of Debut's judgment by proving its claim to the liquidators.

[136] That of course still poses a problem for the liquidators.

[137] The liquidators therefore seek a direction pursuant to s 284(1)(a) of the Act that any belated claims made by the trustees in the liquidation be valued at zero; that they need not make provision for any claims that may be submitted in the liquidation by

the trustees, and do not have to take any further steps to notify the trustees of their ability to file claims in the liquidation.

[138] The relevant parts are:

> **284 Court supervision of liquidation**
>
> (1) On the application of the liquidator, a liquidation committee, or, with the leave of the court, a creditor, shareholder, other entitled person, or director of a company in liquidation, the court may—
>
> (a) give directions in relation to any matter arising in connection with the liquidation:

[139] In considering whether to exercise such a power, I once more adopt the same course as Downs J in *Madsen-Ries v Greenhill*.[41] Downs J considered the previous case law surrounding s 284(1)(a) and ultimately declined to make an order setting any claims by related third parties at zero.

[140] The basis for that decision was uncertainty over whether s 284(1)(a) provided a court with jurisdiction to override the contractual rights of third parties.[42] Looking at the context of the Act, Downs J noted that several provisions gave the Court express power to override contractual rights, while s 284(1)(a) was stated ambiguously.[43] He reasoned that Parliament would likely not have intended such a broad power to be granted to the Court without expressly providing for it.[44] Moreover, decisions of Venning J[45] and Paterson J,[46] suggest that s 284(1)(a) does not provide a Court with jurisdiction to alter the contractual rights of third parties.

[141] I agree. The preferred approach, as adopted by both Venning J[47] and Downs J,[48] is to approach compensation by way of an interim judgment. I will then reserve leave to the liquidators to re-apply to the Court for an increase in quantum if the trustees seek and succeed in proving their unsecured debt in the liquidation.

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41 *Madsen-Ries v Greenhill* [2016] NZHC 3188, [2017] NZCCLR 6.
42 At [120].
43 At [119].
44 At [120].
45 *McGreal Floor Coverings Ltd (in liq) v McGreal* [2014] NZHC 2884.
46 *Re HIH Casualty & General Insurance (NZ) Limited* HC Auckland CIV 2003-404-2838, 17 December 2003.
47 *McGreal Floor Coverings Ltd (in liq) v McGreal* [2014] NZHC 2884 at [25].
48 *Madsen-Ries v Greenhill* [2016] NZHC 3188, [2017] NZCCLR 6 at [120].

Result

[142] I find Mr Cooper has breached his duties to Debut under ss 131(1), 135(b) and 136 of the Act.

[143] I also make the following orders:

(a) Under s 301(1)(b)(ii) of the Act, Mr Cooper is required to make a contribution in the sum of $280,000 towards the assets of Debut.

(b) Under ss 292 and 294(5) of the Act, the payments made by Debut to Mr Cooper totalling $34,129.54, are set aside as voidable transactions. Mr Cooper is also required to repay that amount to the liquidators.

(c) Under s 299(1) of the Act, the GSA entered into between Debut and the Trust, dated 22 March 2013, is set aside as against the second defendants, only to the extent of the awards made against Mr Cooper in this judgment.

(d) Leave is granted to the liquidators to re-apply to the court for an increase in compensation if the trustees of the L and T Cooper Trust succeed in proving in the liquidation as unsecured creditors.

[144] Costs would ordinarily follow in favour of the liquidators on a category 2B basis, together with disbursements. To address this point, the liquidators are to file and serve submissions no later than Thursday, 29 March 2018 and any response is to be filed 21 days later.

Hinton J