IN THE COURT OF APPEAL OF NEW ZEALAND

CA198/2015
[2016] NZCA 103

BETWEEN	VIVIEN JUDITH MADSEN-RIES AND DAVID STUART VANCE AS LIQUIDATORS OF PETRANZ LIMITED (IN LIQUIDATION) First Appellant
	PETRANZ LIMITED (IN LIQUIDATION) Second Appellant
AND	DARRELL WARREN KARANEIHANA PETERA First Respondent
	DIANA JOY PETERA Second Respondent

Hearing:	11 November 2015
Court:	Winkelmann, Courtney and Clifford JJ
Counsel:	N H Malarao and K M Wakelin for Appellants No appearance for Respondents
Judgment:	8 April 2016 at 3 pm

JUDGMENT OF THE COURT

The appeal is dismissed.

REASONS OF THE COURT

(Given by Clifford J)

Introduction

[1] This is an appeal against a decision of Lang J in the High Court that salaries paid to the respondents, Mr and Mrs Petera, by the second appellant, Petranz Limited (in liquidation) (Petranz), were fair to Petranz when paid.[1] The issue on this appeal is whether the Judge, in reaching that conclusion, gave appropriate consideration to the very poor financial situation of Petranz at the time the remuneration was paid.

Background

[2] Petranz was a road transport business. It operated three trucks and specialised in moving containers. Mr Petera drove one of the trucks. Petranz employed drivers to drive the other two trucks. Mrs Petera looked after its administrative needs. Petranz went into liquidation on 30 January 2009. At liquidation, its only debt of real significance was its liability for unpaid taxes. That debt, including penalties, comprised $120,555.33. Other creditors were owed some $12,000.

[3] The appellants, the liquidators of Petranz and Petranz itself, sued Mr and Mrs Petera as Petranz's directors and shareholders. They claimed various breaches of duty and that the Peteras owed Petranz on current account (as shareholders) and for unfair remuneration (as directors).

[4] The Judge first found that the Peteras owed Petranz a total of $140,134.70 on their current accounts.[2] The Judge declined the appellants' application for the repayment of directors' remuneration.[3] The Judge went on to find the Peteras had, as alleged, breached duties they owed Petranz under the Companies Act 1993 (the Act), including the s 135 duty not to trade recklessly.[4] The Judge also found that they had failed to keep proper accounting records as required under s 194.[5]

[5] In terms of quantum for the breach of directors' duties, the liquidators sought recovery from the Peteras of $453,003.33 made up of $132,355.69 for the creditors'

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1 *Madsen-Ries v Petera* [2015] NZHC 538.
2 At [46].
3 At [48]–[51].
4 At [56]–[71].
5 At [72]–[82].

claims together with $280,647.64 for the liquidators' costs up to the start of trial and $40,000 for the liquidators' costs in relation to the trial.[6]

[6] Lang J did not accept the liquidators' approach. He considered that it ignored the language used in ss 300 and 301 and that it would encourage liquidators and their legal advisers to adopt an approach to litigation of this type that was neither cost-effective nor proportionate.[7] The Judge considered the issues were the extent to which Mr and Mrs Petera should be required to compensate Petranz for allowing it to continue trading when they knew it was unable to meet its tax obligations, and their appropriate personal liability for failing to keep adequate accounting records.[8]

[7] Lang J concluded that Petranz was probably insolvent by September 2005[9] and that by no later than 31 July 2006 there was no realistic prospect of it trading on.[10] He determined that Mr and Mrs Petera should be required to compensate Petranz for the losses the Commissioner of Inland Revenue (the Commissioner) suffered after that date: $53,217 on account of GST and $11,491 on account of income tax.[11] He ordered that Mr and Mrs Petera should be personally responsible for the Company's debts in the sum of $20,000 on account of their failure to keep proper financial records.[12]

[8] We endorse those conclusions. If the liquidators' claims had succeeded, the Peteras would have been liable to pay a total of $593,138.03 to Petranz. Given Petranz's debts to its creditors, that is a surprisingly high amount. At the hearing of this appeal Mr Malarao, counsel for the appellants, acknowledged that if the Peteras had been in a position to pay that amount, the unusual situation would have arisen that Petranz would (notwithstanding its liquidation) likely have had surplus funds and have been in a position to make a distribution to the Peteras. In our view, that

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6 At [92]. There appears to be a discrepancy in the calculation of the creditors' claims between the figure provided here and the figure provided at [4], but this is minor and unimportant given the outcome of the appeal.
7 At [93].
8 At [94]–[108].
9 At [14]–[17].
10 At [104]–[105].
11 At [105].
12 At [108].

confirms that the liquidators' approach involved a degree of double counting and that Lang J approached the matter correctly, both in terms of rejecting the liquidators' approach and in terms of assessing the appropriate compensation for the breach of the s 135 duty.

The challenged decision

[9] Section 161 of the Act allows directors to approve their remuneration as directors, or in any other capacity, provided they certify that remuneration is fair to the company.

[10] Under s 161(5) of the Act, directors who receive remuneration:

> (a) that has not been approved by them in terms of the s 161 procedures; or
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> (b) which has been so approved, but where reasonable grounds did not exist for the fairness certificate,

are personally liable to repay that remuneration, save to the extent they establish that it was fair to the company.

[11] The Judge considered the liquidators' application for the repayment of salaries in the following section of his judgment:

> [48] The liquidators also challenge Mr and Mrs Petera's entitlement to receive the salaries that they declared for taxation purposes, and in respect of which the company paid PAYE. …
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> [49] There can be no dispute that Mr and Mrs Petera failed to comply with the requirements of s 161 when they caused the company to pay the salaries. Mr Malarao points to numerous authorities confirming that the issue in this context is not whether the payments were fair in a general sense so far as Mr and Mrs Petera are concerned, but rather whether they can properly be regarded as being fair to the company having regard to the actual and contingent creditors of the company at the time they were made. Payments to a director may not be regarded as being fair to a company when they are made at the expense of the company's creditors.
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> [50] I acknowledge the liquidators' concerns regarding the payment of wages or salaries to the company's directors during a period in which the company was unable to meet its tax obligations. I consider, however, that

> they are answered to some extent by the fact that the company paid PAYE in respect of the payments. To that extent the debt owing to the Commissioner did not become larger during the period in which the payments were made. More importantly, Mrs Petera's unchallenged evidence was that during this period Mr Petera worked 60 to 70 hours per week overseeing the company's operations and driving one of the company's trucks. Mrs Petera worked approximately 20 hours per week attending to the administrative needs of the company.
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> [51] I consider that the company gained full value from the work carried out by Mr and Mrs Petera notwithstanding the fact that the company's liability for GST continued to increase during the same period. In particular, the company was able to derive profit from Mr Petera's work because it was able to charge customers for the driving duties that he undertook on the company's behalf. Its administrative needs were fulfilled by Mrs Petera. I therefore consider that Mr and Mrs Petera have proved that the salaries they received and declared were fair to the company at the time they were made. The liquidators' claims under this head fail as a result.
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> (Footnote omitted.)

The appeal

[12] The appellants argue that Lang J erred in fact and/or law by finding:

(a) That the salaries were fair to Petranz when they were made:

(i) in the face of substantial existing debts owed by Petranz to the Commissioner; and

(ii) at a time when new debts became owing by Petranz to the Commissioner.

(b) That the fact that Petranz paid PAYE on the salaries "to some extent" answered the liquidators' concern that the salaries were paid at the time Petranz was unable to meet its tax obligations.

(c) That the test under section 161 is primarily determined by an assessment as to whether Petranz received "full value" in terms of hours worked vis-à-vis salaries paid out.

[13] For the appellants, Mr Malarao submitted that the requirement in s 161(1) for directors to be satisfied that remuneration paid to directors was "fair to the company"

was a reflection of the directors' fiduciary duty of good faith codified in s 131. In terms of the dicta in *Nicholson v Permakraft (NZ) Ltd*,[13] the directors of a company of doubtful solvency therefore owe a duty to creditors to consider their interests when determining the fairness of director remuneration.[14] The appellants see Lang J's decision as inconsistent with established High Court authority to that effect.

[14] The appellants do not challenge the appropriateness of the remuneration in terms of the work done. Rather they argue that since the company was insolvent at the time, it could not be fair to creditors to continue to pay the directors anything, unless it was for work done toward stopping the company trading and preserving the position of creditors. Thus, Lang J was wrong to find that the test under s 161 was primarily determined by an assessment as to whether the company received "full value" in terms of hours worked vis-à-vis salaries paid.

Analysis

Overview

[15] The liquidators' central proposition is that the duty under s 161 to certify as to fairness is a reflection of directors' 131 fiduciary duty and therefore creditor interests must be considered. We do not accept that proposition.

[16] The scheme of the Act is that creditors' interests are a relevant consideration for directors where the directors authorise distributions and other transfers of benefit by a company to its shareholders. In those circumstances the Act uses the solvency test, not the concept of fairness, to protect creditor interests. Where directors are called upon to authorise transactions in which the interests of the company on the one hand, and its directors or shareholders on the other, may diverge (including the payment of their remuneration), the Act uses the concept of fairness. The issue for directors in those circumstances is fairness as between directors and the company.

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13 *Nicholson v Permakraft (NZ) Ltd* [1985] 1 NZLR 242 (CA).

14 It is difficult to express the proposition in *Nicholson* with a great degree of precision: see the discussion in Peter Watts, Neil Campbell and Christopher Hare *Company Law in New Zealand* (2nd ed, LexisNexis, Wellington, 2016) at ch 17.1. The issue here is the correctness, or otherwise, of the liquidators' characterisation of the duty under s 161 as, in effect, a subset of the duty of good faith under s 131. Mr Malarao did not draw any connection between the s 161 "fairness" test, and the insolvent trading provisions of ss 135 and 136 of the Act.

When certifying fairness, including where required by s 161, directors do not need to consider creditor interests. Directors may nevertheless be liable to contribute to an insolvent company's assets to reflect losses attributable to the payment of director remuneration and, in turn, a company's failure to meet its obligations to creditors. Such liability could arise under s 301, by reference to a breach of the s 135 directors' duty not to trade recklessly. It is to be remembered that, in the context of that duty, the decision of directors to "purchase" services from one of their number is no different from any other trading decision they make.

[17] We set out below the rationale for those conclusions. We start with the role of the solvency test in the scheme of the Act. We then contrast the role of the solvency test and that of fairness certification. The different roles played by those two aspects of the Act lead us to the conclusions we have just foreshadowed.

Directors' duties and the solvency test

[18] Prior to the passage of the Act in 1993, there was no statutory statement of the duties of the directors of a company. Rather those duties had to be discerned from a large volume of complex case law. In its 1987 discussion paper the Law Commission saw that as undesirable.[15] The Law Commission was concerned with what it saw as the low standards of care and skill that had been imposed on directors.[16] The Law Commission was also concerned to clarify the extent to which directors owed duties to the company or to its shareholders.[17] In the context of the Court of Appeal decision in *Nicholson*, the Law Commission considered directors should not owe duties to creditors in circumstances of near insolvency.[18]

[19] The directors' duties provisions of Part 8 of the Act, and particularly the codification of directors' duties now found in ss 131–138, are the statutory resolution of those issues. Pursuant to s 169(3) of the Act, the duties of directors under ss 131, 133, and 135–137 are duties owed to the company and not to shareholders.

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15 Law Commission *Company Law: A discussion paper* (NZLC PP5, 1985) at [191].
16 At [192].
17 At [206]–[211].
18 Law Commission *Company Law Reform and Restatement* (NZLC R9, 1989) at [220].

Speaking of the position of creditors as regards those duties, the Law Commission wrote:[19]

> 217 In particular, we are of the view that it is wrong in principle to impose fiduciary duties upon directors which are owed directly to creditors of the company. Any such extension of directors' duties would unacceptably dilute the scheme of director accountability under the draft Act.
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> …
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> 219 Directors owe a specific duty to the company not to take unreasonable risks of breaching the solvency test (section 105). Where that duty is breached, liability is owed to the company and may be enforced by the company or by a shareholder suing derivatively or, after insolvency, by the liquidator. Creditors will not have standing to obtain a remedy for breaches of the solvency duties owed to the company. To provide such a remedy would be to undermine the statutory system for liquidations. …
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> 220 This is an area of law which has recently been considered in New Zealand and Australia in *Nicholson v Permakraft (NZ) Limited* [1985] 1 NZLR 242 and *Kinsela v Russell Kinsela Pty Limited* 1986 4 CLC 215. The draft Act is consistent with these cases but in so far as they may suggest that in cases of near insolvency creditors are owed and can enforce duties directly against directors, the draft Act would depart from them.
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> …
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> 222 The draft Act would set the duties owed by directors to the company in cases of near insolvency at the standard of unreasonable risk provided for in section 105.[20]

[20] Although not all of the recommendations of the Law Commission were carried over into the new Act,[21] the overall scheme of the directors' duties provisions, and their relationship to the interests of creditors as reflected in that passage, is as envisaged by the Law Commission.

[21] In addition to discharging their general duties, and in particular that found in s 135, the directors of a company are required to certify that the company satisfies the solvency test prior to:

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19 Law Commission, above n 18.

20 Section 105 was not, we acknowledge, enacted in the form recommended by the Law Commission: Law Commission, above n 18, at 241. Its equivalent is found in s 135 of the Act.

21 For example, s 103 has no equivalent in the Act: Law Commission, above n 18, at 241. Similarly the Law Commission saw inclusion of the "*Recovery in other cases*" provisions in ss 297–301 of the Act dealing with liquidation as being unnecessary given the general scheme of the Act as regards directors' duties and the rights given to both the company and to its shareholders to enforce those duties: Law Commission, above n 18, at [214]–[222]. Importantly, s 301 gives creditors the right themselves to enforce those duties, albeit that they are owed to the company. Here, the liquidators relied on s 301, as well as s 300, for the orders they sought.

(a) authorising a distribution (s 52);

(b) approving or continuing a discount scheme (s 55);

(c) exercising an option to redeem a share (s 70); and

(d) providing financial assistance to shareholders (s 77).

[22] Section 56 of the Act imposes liability on both shareholders and directors for the repayment of distributions made when a company does not satisfy the solvency test. It does so in the following terms:

> **56 Recovery of distributions**
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> (1) A distribution made to a shareholder at a time when the company did not, immediately after the distribution, satisfy the solvency test may be recovered by the company from the shareholder unless—
>
> (a) the shareholder received the distribution in good faith and without knowledge of the company's failure to satisfy the solvency test; and
>
> (b) the shareholder has altered the shareholder's position in reliance on the validity of the distribution; and
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> (c) it would be unfair to require repayment in full or at all.
>
> (2) If, in relation to a distribution made to shareholders,—
>
> (a) the procedure set out in section 52 or section 70 or section 77, as the case may be, has not been followed; or
>
> (b) reasonable grounds for believing that the company would satisfy the solvency test in accordance with section 52 or section 70 or section 77, as the case may be, did not exist at the time the certificate was signed,—
>
> a director who—
>
> (c) failed to take reasonable steps to ensure the procedure was followed; or
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> (d) signed the certificate, as the case may be,—
>
> is personally liable to the company to repay to the company so much of the distribution as is not able to be recovered from shareholders.
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> …

[23] Subsection (5) of s 56 allows those repayment obligations to be calibrated by reference to the solvency test:

> (5) If, in an action brought against a director or shareholder under this section, the court is satisfied that the company could, by making a distribution of a lesser amount, have satisfied the solvency test, the court may—
>
> (a) permit the shareholder to retain; or
>
> (b) relieve the director from liability in respect of—
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> an amount equal to the value of any distribution that could properly have been made.

[24] The place of the interests of creditors in the scheme of the Act is therefore clear. By protecting the interests of the company and shareholders, the general directors' duties provisions indirectly protect creditors. The reckless trading provision in s 135 is expressed by reference to the risk of losses to creditors. In certain limited categories of transaction — those where transactions with shareholders may jeopardise creditor interests — directors are required to certify as to the company's solvency immediately after the transaction to protect the interests of creditors.

Fairness and directors' self-interested transactions

[25] As well as codifying directors' duties and introducing the solvency test to protect directly creditor interests, the Act also reformed the law relating to directors' self-interested transactions.[22] It did so first in general terms, and then more specifically as regards the payment of remuneration or the provision of other benefits to directors, whether in their capacity as such or otherwise. It is in that context (where the interests of directors on the one hand and the company and its shareholders on the other may diverge) that the concept of fairness is used.

[26] The question of director remuneration, as a specific type of self-interested transaction, is dealt with in s 161. As noted, the board may authorise the payment of remuneration to a director, provided that the board is satisfied that to do so is fair to

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[22] The major purpose of the reform was to replace the application to company directors of the rule of equity which made voidable any transaction in which a fiduciary was directly or indirectly interested, irrespective of the merits of the transaction.

the company. Similarly, s 162 creates procedures whereby a company may indemnify and insure its directors. Those procedures also include a requirement that any insurance effected by the directors is fair to the company.[23] There is no statutory definition of the concept of fairness.

[27] The concept of fairness is also used, again undefined, in contexts where directors are required to authorise transactions between the company and its shareholders where the interests of a company and its shareholders may diverge and where the interests of shareholders amongst themselves may diverge. Thus:

(a) Under ss 47 and 49, prior to issuing shares, options and convertible securities, or crediting shares already issued as paid up other than for cash, the board must resolve that the terms and consideration of the issue are fair and reasonable to the company and to all existing shareholders.

(b) Under s 60, prior to offering to acquire shares pro rata (therefore presumptively fair as between shareholders) the board must resolve that the terms and consideration of the offer are fair and reasonable to the company.

(c) Under s 61, prior to offering to acquire shares other than pro rata, the board must resolve that the terms and consideration of the offer are fair and reasonable to the remaining shareholders.

[28] Similar requirements are found in ss 63, 65, 69, 71, 76, 78 and 80 relating to stock exchange acquisitions of shares, redemptions of shares, and financial assistance for the purchase of shares.

Solvency and fairness

[29] Directors must certify both as to solvency and as to fairness in a number of instances:

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[23] Section 162(6).

(a) discount schemes (s 55);

(b) distributions comprising:

(i) share buy-backs (ss 60, 61 and 63);

(ii) share redemptions (s 70); and

(c) the provision of financial assistance to shareholders to acquire shares in the company (s 77).

[30] Those separate requirements reflect the Act's scheme that the solvency test protects the interests of creditors against the risk that directors may improperly distribute or otherwise pay company funds to shareholders at the cost of creditors, while fairness certification is required where directors may approve transactions in which the interests of the company and/or its shareholders may diverge.

Protecting creditors from shareholder waiver of fairness requirements

[31] Another aspect of the Act's scheme confirms the distinct roles of the various requirements for fairness certification and the solvency test. Section 107 of the Act allows the requirement for directors to certify as to fairness before they authorise a range of company actions[24] to be dispensed with if "all entitled persons"[25] agree. Section 107(4) requires any such agreement to be in writing if it is to be valid. As it is the shareholders who authorise those actions and not the directors, the general requirement found in s 52 for the board to certify the company passes the solvency test before a distribution (including a share buy-back) is made, and the more specific requirements for the solvency test found variously in ss 55 (discount schemes), 70 (share redemption) and 79 (financial assistance) would not be triggered when action is authorised under s 107. Accordingly, those requirements are replaced by s 108:

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[24] Paying dividends (s 53); establishing discount schemes (s 55); acquiring shares (ss 59–65); redeeming shares (ss 69–72); and giving financial assistance (ss 76–80): s 107(1)(a)–(e).

[25] An entitled person is a shareholder or one to whom the constitution of the company gives the rights of a shareholder: s 2.

> **108 Company to satisfy solvency test**
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> (1) A power referred to in subsection (1) of section 107 must not be exercised unless the board of the company is satisfied on reasonable grounds that the company will, immediately after the exercise of the power, satisfy the solvency test.

In that way, the Act ensures that the exercise of that shareholder power is subject to the board being satisfied as to solvency, just as if the board was authorising the relevant action itself. Section 108 goes on to provide:

> (4) The provisions of section 56 apply in relation to the exercise of a power referred to in subsection (1) of section 107, with such modifications as may be necessary.

[32] Thus:

> (a) shareholders who receive distributions and other payments authorised under s 107; and
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> (b) directors who fail to certify solvency, or do so without reasonable grounds, with respect to those payments,

will be liable in terms of s 56(1) and (2) respectively, including as "calibrated" for solvency under s 56(5).

Protecting creditors from "unfair" director remuneration

[33] As already noted, the scheme of the Act reflects that in the ordinary course, if a payment of director remuneration is fair to the company, creditor interests would not normally arise. To the extent that they do, the duty not to trade recklessly in s 135 can be seen as recognising those interests. Hence, the Act does not require directors to certify as to solvency (the creditor protection test) when authorising their own remuneration under s 161.

[34] Section 107 includes within the "unanimous assent" actions the authorisation of director remuneration other than as required by s 161(1).[26] Where shareholders relieve directors from the s 161 obligation to ensure that remuneration paid to

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[26] Section 107(1)(f).

directors is fair to the company, potential is created for director remuneration to jeopardise the interests of creditors, particularly in the case of shareholder-directors. For that reason, directors who are not required to certify as to solvency under s 161 if they themselves authorise their remuneration under s 107 must nevertheless do so under s 108(1) to protect creditors.

[35] The liquidators argue that Lang J's decision creates a perverse incentive for shareholder-directors simply to not comply at all with the provisions of the Act relating to the authorisation of remuneration. Mr and Mrs Petera could, as shareholders, have approved their remuneration using the s 107, unanimous consent, process. If they had done so (it is common ground they did not fulfil the formal requirements of s 107(4)), they would have been liable under s 56(2) and (5) to repay that remuneration to the extent it would have caused the company to fail the solvency test. On Lang J's analysis, s 108 is not invoked because they failed to fulfil the s 107(4) requirements, so they need only show the remuneration was fair under s 161 putting to one side the company's financial position.

[36] We acknowledge that that is the legal position. We do not think, however, it is inconsistent with the scheme of the Act or creates any perverse incentive. The creditors have their rights under s 301 directly, or through a liquidator, to enforce their claims for the breach of duties that may arise where directors continue to trade and incur liabilities to creditors when a company is of doubtful solvency or is indeed insolvent. The enforcement of those duties gives the Court the appropriate framework to determine the liability of directors to creditors. Where a company is insolvent, or is on the verge of insolvency, payment of director remuneration will be reflected in company losses and, in turn, in that company's failure to pay its debts. It is the job of the Court where directors' duties are breached to determine the appropriate extent of director liability, as Lang J did. The obvious duplication of claims that arises from the approach the liquidators took against Mr and Mrs Petera confirms our analysis. Moreover, a course of conduct where the shareholder-directors of a closely held company authorised remuneration by reference to distributable profits would give rise to the very real risk for them of that remuneration being seen as a distribution, meaning that the shareholder-directors may be liable to return the remuneration to the company under s 56(1).

[37] We therefore conclude as a matter of principle that the concept of fairness in the Act is one that calls for a consideration of the potentially competing interests of a company and its directors, a company and its shareholders, and shareholders themselves, but not the interests of creditors.

[38] As we have made clear, this is not to say that directors are not also subject to other duties when authorising remuneration, which other duties may require them to consider the interests of creditors in circumstances of financial difficulty. It is only to say that the interests of creditors are not a relevant consideration when assessing fairness under s 161, nor when considering questions of personal liability under ss 161(5) and (6) and 162(8). In this context, we note that the decision of directors to "purchase" services from one of their number is no different from any other trading decision they make in the context of their duty not to trade recklessly.

High Court authorities

[39] We acknowledge the various High Court judgments which were cited by Mr Malarao as authority for his argument. We consider each of them, albeit relatively briefly, in chronological order.

[40] We start with Potter J's decision in *Re Gellert Developments Ltd (in liq)*.[27] At 30 September 1994 Mr and Mrs Gellert had determined that their company should cease trading.[28] Their subsequent shareholders' resolution at 31 December 1995 allocated all the profit up to 30 September 1994 to shareholder salaries.[29] Potter J noted that the shareholders had done so without considering any justification for the level of the salaries paid.[30] She then observed:[31]

> That, as has been previously stated, cannot be criticised in a company which is solvent and where there are no unpaid creditors, but that was not the situation here as I find later in this judgment. I conclude that salaries credited for the 1995 financial year, ie to 30 September 1994, were excessive.

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27 *Re Gellert Developments Ltd (in liq)* (2002) 9 NZCLC 262,942 (HC).
28 At [19].
29 At [18].
30 At [43].
31 At [43].

[41] We note that Potter J did not reason explicitly by reference to the concept of fairness. It is clear that the directors could not have certified as to the continuing solvency of the company after the payment of those salaries. It was the prejudicial impact of those payments on the company's ability to discharge its debts to the claiming creditor that prompted the liquidators' claim. It would appear that Potter J's attention was not drawn to the implications in those circumstances of ss 108 and 56. In our view, s 56 was the appropriate mechanism for recovery of the excessive salaries.

[42] In *National Trade Manuals Ltd (in liq) v Watson* Venning J considered a challenge to shareholder-director remuneration paid by a company put into liquidation by Inland Revenue.[32] The payment had been approved by shareholder's resolution.[33] Venning J found that did not assist. He did so on the explicit basis that s 108 had not been complied with, and that therefore s 56 applied.[34] In our view, his approach conforms with our analysis, and does not support the propositions Mr Malarao advanced.

[43] In *Managh v Jordan* Miller J considered, amongst other things, the fairness of salary payments made under s 161 after a company became insolvent.[35] We acknowledge the Judge did refer to *Nicholson* and *Sojourner v Robb*[36] as authority that directors in those circumstances must take account of the interests of creditors.[37] Nevertheless, he determined the repayment issue on the basis of whether or not the shareholder-director could meet the test of satisfying that the payments were fair to the company, the insolvency aside.[38]

[44] The significance of s 161 of the Act played a very small part in Duffy J's extensive judgment in *Victoria Street Apartments Ltd (in liq) v Sharma*.[39] Moreover, the Judge found that the director in question had breached his fiduciary duties to the

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32 *National Trade Manuals Ltd (in liq) v Watson* (2006) 9 NZCLC 264,163 (HC).
33 At [7].
34 At [43]–[49].
35 *Managh v Jordan* [2010] NZCCLR 4 (HC).
36 *Sojourner v Robb* [2006] 3 NZLR 808 (HC).
37 At [40].
38 At [41]–[42].
39 *Victoria Street Apartments Ltd (in liq) v Sharma* HC Auckland CIV-2009-404-8377, 14 October 2011.

company in authorising the challenged transactions.[40] The Judge also found those actions in breach of s 161, but without any particular analysis.[41] We do not think *Victoria Street Apartments* adds any strength to the liquidators' argument.

[45] In *Richard Geewiz Gee Consultants Ltd (in liq) v Gee*, a liquidator sought the return to the company of salary payments to a director.[42] The company had ceased trading on 30 September 2008.[43] Brown J concluded, by reference to the company's indebtedness at the relevant time to Inland Revenue, that reasonable grounds did not exist for Mr Gee's opinion that the payment of salaries was fair to the company at the date of the certificates.[44]

[46] *Geewiz* provides, therefore, the most direct support for the liquidators' argument of the various cases we were referred to. The authorisation of the salary payments extinguished the debit balance in the shareholders' current account. The directors were, therefore, not only authorising the payment of salary but also the disposition of an asset of the company. The decision was made in the face of clear financial difficulties confronting the company. Brown J later found that Mr Gee had, as pleaded, breached the duties he owed to the company under ss 135[45] and 137.[46] In our view, Mr Gee's liability for those breaches was the appropriate way to determine his responsibility for the company's debts, very much as the Law Commission envisaged.

[47] Therefore, we are not persuaded that these decisions do support the liquidators' argument. Nor have they persuaded us that our in principle conclusion is incorrect.

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40 At [159]–[160].
41 At [158]–[159].
42 *Richard Geewiz Gee Consultants Ltd (in liq) v Gee* [2014] NZHC 1483.
43 At [1].
44 At [59].
45 At [96]–[103].
46 At [104]–[106].

Result

[48] We are satisfied that Lang J made no error of law as regards the application of s 161. We are also satisfied that his assessment of fairness cannot otherwise be challenged.

[49] This appeal is, therefore, dismissed.

Costs

[50] In the absence of any appearance for the respondents, no question of costs arises.

Solicitors:
Meredith Connell, Auckland for Appellants