IN THE HIGH COURT OF NEW ZEALAND
CHRISTCHURCH REGISTRY

CIV- 2014-404-000469
[2015] NZHC 866

IN THE MATTER	of Sections 292-296 and s 299 of the Companies Act 1993
BETWEEN	DAVID ROSS PETTERSON AS LIQUIDATOR OF POLYETHYLENE PIPE SYSTEMS LIMITED (IN LIQUIDATION) Applicant
AND	DAVID CHARLES BROWNE Respondent

CIV-2014-409-000900

IN THE MATTER	of Sections 292-296 of the Companies Act 1993
BETWEEN	DAVID ROSS PETTERSON Applicant
AND	DAVID BROWNE CONTRACTORS LIMITED First Respondent
AND	DAVID BROWNE MECHANICAL LIMITED Second Respondent

Hearing:	3-5 March 2015 / 27 March 2015 - further submissions
Appearances:	B Gustafson and L Van for Applicant D J C Russ for Respondents
Judgment:	29 April 2015

JUDGMENT OF ASSOCIATE JUDGE MATTHEWS

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Introduction

[1] Mr Petterson is the liquidator of Polyethylene Pipe Systems Limited (PPS). He was appointed by the High Court at Christchurch on 5 October 2009 on the application of McConnell Dowell Constructors Limited (McDow).

[2] He has brought the subject proceedings as a result of his investigation into the affairs of the company. The first proceeding, CIV-2014-409-469 (the 469 proceeding), follows service on Mr Browne of two notices under s 294 of the Companies Act 1993 alleging, respectively, that a payment to him of $340,600 was voidable under s 292 and that a charge given to him by PPS was voidable under s 293. Mr Browne gave a notice of objection to each notice, under s 294(3).

[3] Mr Petterson initially sought four orders:

(a) that the payment to Mr Browne of $340,600 by PPS is voidable under s 292 of the Companies Act 1993;

(b) that the charge granted by PPS in favour of Mr Browne under a general security agreement dated 28 July 2008 be set aside under s 293;

(c) in the alternative, that the general security agreement be set aside under s 299; and

(d) that Mr Browne repay to PPS all amounts received by him pursuant to the general security agreement, including the sum of $340,600 sought under the first order, a further sum of $201,306 paid to him as secured creditor, and any other amounts the Court deems appropriate.

[4] After cross-examination of four deponents, Mr Gustafson advised that the liquidator no longer sought orders under (a) and (b), with the result that he no longer sought an order that Mr Browne repay the sum of $340,600. The balance of the application is opposed by Mr Browne.

[5] The second proceeding, CIV-2014-409-900 (the 900 proceeding) arises from Mr Petterson's service on David Browne Contractors Limited (DBC) and on David

Browne Mechanical Limited (DBM) of notices under s 294 of the Companies Act by which he sought to set aside payments made to those companies as voidable. The payment to DBC was $565,303, and the payment to DBM was $347,634.

[6] Neither DBC nor DBM responded to the notices by making objections in accordance with the relevant statutory procedure within 20 working days of service. The automatic consequence is that the payments are set aside.[1] It was established in evidence that the notices were served at the registered office of the companies, their accountant's office, but were filed by a staff member who received them. They were not drawn to the attention of Mr Lay, their accountant. Nor were they referred to any officer of DBC or DBM.

[7] As a result Mr Petterson seeks orders under s 295(a) of the Companies Act directing DBC and DBM to repay to him the sums they respectively received. The applications are opposed by DBC and DBM.

[8] By a consent order, evidence on each application may be considered on the other. The applications were heard together. Some of the issues to be decided arise on both claims. It is also accepted that as Mr Browne was at all times a director of PPS, DBC and DBM, any finding in relation to his state of mind will also be a finding in relation to each company.

Relevant facts not in dispute

[9] PPS is one of numerous companies (presently 40) owned by Mr Browne, his wife, the Browne Family Trust, and other Browne family interests. The company Mr Browne first set up was DBC. It is a mechanical services contractor. It installs services (for example, air conditioning) into buildings. DBM undertakes gas engineering services.

[10] PPS was incorporated in 1992. It supplies high density polyethylene pipes and fittings for use in the wastewater, stormwater and irrigation industries. It also undertakes butt welding and electrofusion of polyethylene pipes.

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1 Companies Act 1993, s 294(3).

[11] Late in 2006, McDow contracted with the Christchurch City Council to construct a 4.8 kilometre sewer outfall pipe. In March 2007, McDow contracted with PPS to weld together sections of the pipe prior to its installation.

[12] McDow took out a contract works insurance policy in June that year, but PPS did not insure itself against any liability that might arise under the contract.

[13] The contract contained three provisions which are of relevance to the present case:

> 9.1 Any defects, omissions or errors in the Subcontract Works will, prior to the expiration of the maintenance period stipulated in the Head Contract and upon notification by the Contractor to the Subcontractor, be made good to the satisfaction of the Contractor by the Subcontractor at its own cost within 10 Working Days from delivery of the notification in writing, or within such other time or times as may be stipulated in the notice.
>
> 9.2 In the case of any default by the Subcontractor in complying with any notification in 9.1 above, the Contractor may, in addition to any other rights or remedies, make good the defects, omission or error itself or through other contractors or agents. The cost of so doing shall be recoverable from the Subcontractor.
>
> ...
>
> 11.1 The Subcontractor will protect and indemnify the Employer and the Contractor against all losses, claims, costs, charges, expenses and damage arising out of, in connection with, or in consequence of the Subcontract Works unless and to the extent the losses, claims, costs, charges, expenses and damage is caused by the fault or neglect of the Contractor its servants or agents.

[14] The work required on the part of PPS was carried out. The piping itself was supplied by PKS-Frank NZ Limited (PKS-Frank) which manufactures polyethylene pipes under licence from a German company, Frank GmbH.

[15] Once the pipeline had been constructed by PPS into 360 metre long sections from shorter lengths, it was laid by McDow. The pipeline design, in which PPS played no part, required the finished pipe to be weighted down on the seabed by 15.2 ton concrete blocks attached at 6 metre centres.

[16] Once the pipe was on the seabed, it was found that three of the welded joints had failed, though not all at once.

[17] The following sequence of events then occurred:

24 January 2008 - McDow notified PPS of alleged defective work, the failure of pipe string 1 weld 151.

8 May 2008 - McDow notified PPS that a second weld had failed, pipe string 6 weld 32.

20 June 2008 - McDow notified PPS it had suffered significant losses from what it believed was defective work on the part of PPS, and advised it was calculating the quantum of a claim against PPS under the contract.

26 August 2008 – McDow advised PPS of a claim for $2,552,671.14 for the first weld failure, with a breakdown of the claim.

5 September 2008 – McDow wrote to PPS giving a breakdown of the loss claimed in respect of the second weld failure. The sum claimed was quantified at $449,524.19.

19 December 2008 – McDow notified PPS of the loss claimed in relation to third weld failure (the date of notification of this failure is unclear). The claim was quantified at $394,558.35.

19 January 2009 – McDow issued a notice of adjudication under the Construction Contracts Act 2002.

15 May 2009 – An adjudication claim was served in the sum of $3,396,753.50.

20 July 2009 – Adjudication was given in favour of McDow in the sum of $2,996,924.49.

29 July 2009 – Mr Browne appointed Glen Stapely, a chartered accountant as a receiver of PPS pursuant to a general security agreement granted in his favour on 28 July 2008.

5 October 2009 – Mr Petterson was appointed as liquidator by the Court on the application of McDow.

[18] This chronology relates only to the contract between PPS and McDow, the claims which arose from it, their resolution, and the receivership and liquidation of PPS. While that was going on, other steps were being taken in relation to certain indebtedness PPS had to DBM, DBC and Mr Browne. These gave rise to the payments and the charge which are challenged in these proceedings. The dates of key steps in this process are interspersed among the dates of the key steps in the McDow/PPS dispute.

[19] So too, are various steps relevant to the question of whether PPS was covered by insurance held by McDow in respect of the claims made against it, and a separate unrelated claim by a company called Bosch against PPS in respect of a different project. Bosch issued proceedings against PPS and PPS counterclaimed. After 10 days of hearing in the High Court the case was settled in December 2011 by the claim being discontinued, and Bosch paying PPS $170,000.

[20] PPS also entered a further transaction during this period for the sale of some of the shares it held in PKS-Frank at the amount of a valuation provided by PPS's accountant, Mr Lay. I also place this transaction in the sequence of events, though more for completeness than for relevance for reasons I give later in this judgment.

[21] The three payments and the charge which are challenged in these proceedings need to be considered in the context of the McDow claim process because, in essence, Mr Petterson's case is that at no point could PPS meet McDow's claims. As a result, the charge in favour of Mr Browne should be set aside and the payments made should be recovered in the liquidation under one or other of the relevant sections of the Companies Act.

[22] It is, therefore, of assistance to reproduce one chronology of events, using the above sequence as a starting point and interposing the key dates of transactions in the restructuring of the financial affairs of PPS. The latter are shown in italics.

> **24 January 2008 -** McDow notified PPS of alleged defective work, the failure of pipe string 1 weld 151.

8 May 2008 - McDow notified PPS that a second weld had failed, pipe string 6 weld 32.

20 June 2008 - McDow notified PPS it had suffered significant losses from what it believed was defective work on the part of PPS, and advised it was calculating the quantum of a claim against PPS under the contract.

30 June 2008 *– Directors of PPS resolved that it will repay advances in a total of $1,253,537 to DBC, DBM and Mr Browne.*

1 July 2008 *– Directors of PPS issued a solvency certificate stating they believe PPS is solvent in terms of s 4 of the Companies Act.*

4 July 2008 *– Mr Lay provided a valuation of the shares in PKS-Frank which PPS is to transfer to the Browne Family Trust.*

28 July 2008 *– Directors of PPS approved new borrowings in unspecified amounts by PPS from Mr Browne, to be secured by a general security agreement (GSA). A facility loan agreement was signed between PPS and Mr Browne for advances, and later registered.*

21 August 2008 *– PPS directors resolved to sell the majority of the shares it held in PPS-Frank to the Brown Family Trust at valuation, $309,543.*

26 August 2008 – McDow advised PPS of a claim for $2,552,671.14 for the first weld failure with a breakdown of the claim.

29 August 2008 *- $700,000 transferred from the bank account of DBC to PPS.*

2 September 2008 *- PPS made the following payments:*

to DBC $565,303

to DBM $347,634

to Mr Browne $340,600

(which total the aggregate sum referred to in the entry for 30 June, and are three of the sums sought in this case)

5 September 2008 – McDow wrote to PPS giving a breakdown of the loss claimed in respect of the second weld failure. The sum claimed was quantified at $449,524.19.

19 December 2008 – McDow notified PPS of the loss claimed in relation to the third weld failure. The claim was quantified at $394,558.35.

19 January 2009 – McDow issued a notice of adjudication under the Construction Contracts Act 2002.

16 February 2009 *– Mr Browne demanded repayment by PPS of $450,000 secured by his GSA.*

15 May 2009 – An adjudication claim was served in the sum of $3,396,753.50.

20 July 2009 – Adjudication delivered in favour of McDow in the sum of $2,996,924.49.

29 July 2009 – Mr Browne appointed Glen Stapely, a chartered accountant as a receiver of PPS pursuant to the general security agreement granted in his favour on 28 July 2008.

5 October 2009 – Mr Petterson was appointed as liquidator by the Court on the application of McDow.

Prior to July 2010 – *Receiver, Mr Stapely, paid Mr Brown $201,316 as a creditor secured under his GSA.*

Claim 469 against Mr Browne

Discussion of the notices issued under s 292 and s 293

[23] The first order sought in this claim was that the payment to Mr Browne of $340,600 by PPS is voidable under s 292 of the Companies Act 1993. Although this claim is not pursued, I will discuss the validity of the notices issued to Mr Browne and those issued to DBC and DBM as this is relevant in the context of the orders Mr Petterson seeks against the companies under s 295.

[24] The relevant subsections of s 292 provide:

> **292 Insolvent transaction voidable**
>
> (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.
>
> ...

[25] Mr Russ accepts that the payment was a transaction in terms of the section, and was made within the specified period (two years prior to the liquidation). He says, however, that the company was, at all times relevant to the transactions under scrutiny, not only able to pay its due debts, but also solvent in terms of the definition in s 4 of the Companies Act. In fact, it was established in evidence that when the payments were made on 2 September 2008, PPS did not have any debts apart from the advances by DBC and DBM, repayment of which is in issue. PPS had substantial cash reserves on deposit with its bank, sufficient to repay these advances.

[26] However, it had notice of claims from McDow, the first of which had been quantified in a sum which PPS could not pay from cash or realisation of other assets. So if the claim was "a due debt" in terms of s 292(1)(b), all the payments would have been voidable, as would the GSA granted to Mr Browne several weeks earlier.

[27] That was the basis on which Mr Petterson issued notices under s 294 seeking to set aside the payments to Mr Browne, DBC and DBM, and the charge in favour of Mr Browne, under ss 292 and 293 respectively. Quite correctly, in my opinion, Mr Petterson withdrew the application under s 292 in respect of the payment to Mr Browne on 2 September 2008. The sum claimed by McDow was not then owing, let alone due. Mr Gustafson submitted that in determining whether a company was able to pay its due debts at the time of entering an insolvent transaction under s 292 or immediately after a charge is given in terms of s 293, the Court may look at a short period on either side of these times. I accept that is established law. However, for the reasons which follow, the first point in time, in my view, when there was a debt due to McDow was when the decision on the adjudication was delivered on 20 July 2009, over 10 months after the transactions under scrutiny. That is well outside any reasonable time surrounding the date of the transaction in question.

[28] Prior to that, liability for the claims by McDow was denied by PPS. Until liability (and quantum) were established, no sum was owing by PPS to McDow under the contract. This is clear from the contract. First, clause 9.2 of the contract provides that the cost of making good defects, omissions or errors in the subcontract works is recoverable from the subcontractor. At no point prior to the adjudication was it established that there was any defect, omission or error in the subcontract works. Therefore, at no time prior to that was the cost recoverable by McDow from PPS, and therefore owing (let alone due).

[29] Secondly, the indemnity given by PPS to McDow under clause 11.1 of the contract only applies if the losses were not caused by PPS. This point was put in issue by PPS at the outset and, again, was not decided until the decision in the adjudication process.

[30] As I have said, Mr Petterson's response to this flaw in the notices he had given under ss 292 and 293 was to withdraw the notices under ss 292 and 293 against Mr Browne. However, Mr Petterson was unable to take this step in relation to the notices issued against DBC and DBM because, as I have said, those companies did not respond to the notices and therefore, under s 294(3), the payments to those companies were automatically set aside. Mr Petterson did not elect to

withdraw his claim for repayment of those sums under s 295, notwithstanding the fact that the notices to DBC and DBM were based on a premise which was wrong. I return to this point when considering the claims against those companies.

The issues to be decided

[31] The case for the liquidator against Mr Browne which remains for decision is whether the GSA granted in his favour should be set aside under s 299, and if the answer to that question is yes, whether the elements of s 296(3) are established, preventing the Court from ordering recovery of the payments made to Mr Browne under his security. It is for the liquidator to establish the former, but for Mr Browne to establish the latter. Initially the liquidator said that if he succeeds on these issues, an order should be made under s 295(a) directing payment to him of the sum received by Mr Browne from the receiver, under his security. Mr Browne says that even if that point is reached, the Court has a discretion not to order repayment under s 295. This is refuted by Mr Petterson who says that once transactions are set aside, an order must be made under s 295.

[32] Because s 295(a) only applies where a charge is set aside under s 294, not s 299, Mr Gustafson now says that repayment should be ordered under s 299(3) which provides for the Court to make "such other orders as it thinks proper for the purposes of giving effect to an order under this section".

[33] Mr Petterson puts in issue whether the advance of $700,000, made on 29 August 2008, was made by Mr Browne, as he claims, or by DBC.

[34] Mr Russ puts in issue whether an order may be made under s 299(1) after a receiver has been appointed under a security.

[35] In logical sequence the issues to be decided in relation to Mr Browne are:

(1) Did Mr Browne make the advance of $700,000 to PPS?

(2) Can an order be made under s 299(1) after a receiver has been appointed under a security?

(3) Should the GSA granted by PPS to Mr Browne be set aside under s 299?

(4) If so:

(i) Can the Court order repayment under s 299(3)?

(ii) Is the Court prevented from ordering repayment of the sum he received from the liquidator under his charge ($201,306) by s 296(3)?

First issue: Did Mr Browne make the advance of $700,000 to PPS on 29 August 2008?

[36] As I have recorded, DBC paid $700,000 to PPS on 29 August 2008. Mr Petterson says, therefore, that Mr Browne did not personally make this advance and, as a result, he did not make any advance under his security and the purported repayment to him pursuant to the security should therefore be set aside. Mr Browne accepts that DBC transferred this sum to PPS from its account. He says, however, that this was, in substance, an advance by him.

[37] Evidence for Mr Browne on this point was given by Mr S A Carey. He is a chartered accountant and a partner and director of Grant Thornton New Zealand Limited. He has 23 years experience as an accountant and appropriate formal qualifications. He specialises in expert financial investigation, business and company valuations, accounting opinions and independent reports, arbitration and other dispute resolution work. He is suitably accredited as an expert to give opinion evidence on this issue.

[38] Mr Carey notes the following facts relevant to his opinion:

(a) On 28 July 2008, PPS resolved to borrow funds from Mr Browne to "assist its working capital and cashflow requirements". The resolution expressly records that Mr Browne was willing to lend further funds to the company against the registered general security and approved the

entry of the company into a loan facility agreement and general security agreement.

(b) As Mr Carey puts it, "Mr Browne appears to live his identity through DBC and does not distinguish between the individual and separate legal entity of the company". Mr Browne does not have a personal bank account. Mr Carey says that on reviewing the ledger records for DBC, there are numerous items of personal expenditure made by DBC on behalf of Mr Browne, which is consistent with Mr Browne's evidence that all his personal expenditure is charged to a credit card in the name of DBC, and then debited to his current account.

(c) Interim management accounts prepared for PPS by Mr Lay to 31 December 2008 record "Advance – D C Browne – (secured)" under current liabilities, in the sum of $450,000.[2] As there is no entry in the comparatives column for the previous year, this transaction took place between 1 April 2008 and 31 December 2008.

(d) The statement of financial position of PPS as at 31 March 2009 records an advance from D C Browne, secured, in the sum of $523,579.

[39] Mr Carey then notes that when the sum of $700,000 was paid into PPS, the entry in the PPS bank statement records "DC DAVID BROWNE CO DBC LIMITED". However, the transfer of $700,000 to PPS is recorded in the DBC general ledger account as an advance to PPS Limited.

[40] Mr Carey analyses a number of other entries and concludes that there is a mismatch between the financial statements for DBC and PPS, PPS recording that Mr Browne advanced the moneys and DBC recording that it advanced them.

[41] Although Mr Carey postulates that the notation on the bank statement which I have recorded might be interpreted as a transfer originating from DBC but for the benefit of David Browne care of that company, I am satisfied from other references

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[2] The figure of $450,000 is derived from the advance of $700,000 and repayment to Mr Browne of $250,000 then owing to him.

in the same phraseology to transfers from DBC that, in fact, this suggestion is incorrect and that the transfer notation records a transfer from DBC itself.

[42] Mr Lay gives an explanation in his affidavit of how the mismatch between the way this transfer was recorded in the accounts of each company occurred. I need not record his explanation. It was dismissed by Mr Carey, and I think correctly. The real issue is whether the transfer of the funds was, in substance, an advance from Mr Browne or, in substance, an advance from DBC.

[43] Mr Carey's conclusion is that, on the basis of only the PPS and the DBC accounts, he was unable to say which correctly reflects the transaction. He therefore looked for assistance from the circumstances surrounding the transactions in order to consider the substance of them rather than the form in which they are recorded. He then concludes:

> For the reasons that I have already stated, I believe that the $700,000 was intended to be an advance from Mr Browne to PPS. All of the surrounding circumstances, including a significant number of key formal documents, support that position. I see no evidence to suggest that DBC was intended to loan moneys to PPS and, in the face of the agreed structure and formal documentation, a loan by DBC would be contrary to what was being done through the restructure.
>
> Putting aside the poor and unhelpful accounting treatments I am satisfied that on balance, the treatment of the $700,000 in the PPS accounts is more likely to be the correct treatment than its subsequent treatment in the DBC accounts.

[44] Mr Carey was not called for cross-examination.

[45] The way a financial transaction is treated in a set of accounts is prima facie evidence of the nature of that transaction. In my opinion though, the Court is entitled to look behind the accounting treatment and examine further evidence on the nature of the transaction if it is called into question, as here. The accounts for PPS accurately reflect the other documentation in relation to the intention of the directors of PPS to borrow $700,000 from Mr Browne. Further, the evidence before the Court shows that DBC was frequently used as an entity through which transactions for Mr Browne were undertaken. Thirdly, although the accounts for DBC do not reflect the nature of the transaction as recorded in the PPS accounts, or the resolution of the

directors of PPS, I accept Mr Carey's expert testimony. I therefore find that the sum of $700,000 was advanced to PPS by Mr Browne personally.

Second issue: Does the Court have jurisdiction to make an order under s 299(1) after a secured creditor has appointed a receiver and the receiver has realised the assets of the company and made payments to the secured creditor?

[46] The following passage appears in Brookers Insolvency Law & Practice:[3]

> it is presumed that [s 299] cannot be used if the security has been realised prior to the commencement of the liquidation.

No authority is cited for this proposition.

[47] In Heath and Whale *Insolvency Law in New Zealand*, the learned authors say, in relation to s 299:[4]

> It is likely that if the secured creditor exercised its security prior to the liquidation of the company then it is entitled to the benefits received notwithstanding that the security or charge might have been set aside as against the liquidator under the section.

Again, no authority is cited for this proposition.

[48] As the chronology shows, Mr Stapley was appointed as receiver well before Mr Petterson was appointed as liquidator. He remained in office after that occurred. Therefore, if these views are correct, Mr Petterson's claim under s 299 must fail.

[49] Counsel made brief reference to this issue in argument and, at my request, filed further more detailed submissions later. Because of the view I have come to in relation to the third issue, whether it is just and equitable that the security to Mr Browne should be set aside, it is not necessary to canvass those submissions and reach a conclusion. It is sufficient to record that neither counsel was able to assist the Court with any case on point, nor has my own research uncovered any authority of assistance.

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3 Brookers Insolvency Law & Practice (online looseleaf ed, Thomson Reuters) at CA299.01.

4 P Heath and M Whale (ed) Heath and Whale *Insolvency Law in New Zealand* (LexisNexis, Wellington, 2011) at [20.76].

[50] Mr Russ referred me to *Mace Builders (Glasgow) Ltd v Lunn*, a case decided under s 322 of the Companies Act 1948 in England.[5] In that case the Court of Appeal found that the section has no application until the company is being wound up, and a decision to set aside the security does not affect payments made under it prior to that order.[6]

[51] Had it been necessary to decide this point I would not have been materially assisted by reference to this case. As Mr Russ accepted, the wording of s 322 is materially different from s 299.

[52] Because it is unnecessary to decide this point, it is preferable to refrain from further comment in a judgment where any conclusion expressed would be obiter.

Third issue: Should the GSA granted by PPS to Mr Browne be set aside under s 299(1)?

[53] Section 299 provides, to the extent relevant:

> **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 –
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> (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
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> (d) another company, that at the time when the security or charge was created, was a related company, -
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> 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,

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5 *Mace Builders (Glasgow) Ltd v Lunn* [1986] Ch. 459; affirmed by *Mace Builders (Glasgow) Ltd v Lunn* [1987] Ch. 191.

6 *Mace Builders (Glasgow) Ltd v Lunn* [1987] Ch. 191.

> 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.
>
> …
>
> (3) The Court may make such other orders as it thinks proper for the purpose of giving effect to an order under this section.
>
> …

[54] Mr Browne accepts that the sole issue to be decided under subs (1) is whether, having regard to the factors described, it is just and equitable to set aside his GSA.

[55] Despite s 299 being enacted in 1993 there are few decided cases under it and none of present relevance. It replaced s 311B of the Companies Act 1955 which was inserted into the Act by the Companies Amendment Act 1980. That section provided that in circumstances differing only slightly from those now required by s 299, a charge could be set aside against a liquidator if the Court considers it just and equitable to do so. The factors to be taken into account under each section are the same, save that the conduct to be examined under the 1993 section reflects the broader range of charge holders whose securities may now be impugned. The difference is immaterial for present purposes. Reference may therefore be made to cases decided under s 311B.

[56] The task of the Court under s 299 is to examine the substance of the transaction under review. In *Re Manson and James Ltd (in liq)*, Savage J said:[7]

> Mr Panckhurst also relied on *Re Mataura Motors Ltd*. He referred particularly to the judgment of Richardson J and submitted, I think correctly, that the case shows that the true test for determining whether the section applies is whether the substance of the transaction brings it within the terms of the section or not. It is the substance of the matter, not the form, that determines whether the transaction is within the section or not and to decide that it is necessary to look at it from a practical and business point of view.
> …

[57] After referring to the facts of *In re Destone Fabrics Ltd*,[8] Savage J said:[9]

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7 *Re Manson and James Ltd (in liq)* (1984) 2 NZCLC 99,092 at 99,095.
8 *Re Destone Fabrics Ltd* [1941] Ch 319.
9 At 99,095.

> Simonds J held that the object and effect of the transaction was not to benefit the company but merely to provide money for the benefit of certain creditors of the company to the prejudice of other creditors. The company was not in substance provided with money but only in form.

[58] In my opinion there are three elements of the circumstances in which the transactions were undertaken, which are material to the decisions made by Mr Browne and the other directors of DBC and DBM.

[59] The first is PPS's financial position. At the time of the transactions under review, PPS had been in business for 16 years. Although profit and loss accounts were not produced, there is no suggestion that PPS was anything other than a profitable company. The statement of financial position as at the balance date immediately preceding the transactions, 31 March 2008, discloses a surplus of assets over liabilities of just under $600,000. The company held cash at Westpac and the ANZ of over $1,500,000. Although accounts payable totalled approximately $643,000, the evidence points to accounts with creditors being current at all times. There is no evidence that suggests otherwise. Nor is there any evidence that suggests that the position of the company had deteriorated in any way between 31 March 2008 and 1 July 2008 when the directors signed a solvency certificate, and 28 July 2008 when PPS granted the GSA in favour of Mr Browne.

[60] Mr Petterson formed the view that PPS was insolvent when the transactions were entered. The solvency of PPS was examined by David Ian Ruscoe, a chartered accountant called by Mr Browne as an independent expert witness. He has considerable expertise and experience as a receiver and a liquidator as has Mr Petterson. He swore an affidavit and was called for cross-examination. He analysed the statements of financial position for PPS for the years ended March 2006 to 2009 inclusive, and a set of management accounts prepared at 31 December 2008. On his analysis of the accounts, PPS had significant net assets at each date except March 2009. Although at all dates save December 2008, it had a shortfall in working capital once the shareholders' current accounts were properly recast in the accounts as current liabilities, Mr Ruscoe said that the company had the support of its shareholders by way of advances, and in the absence of evidence to the contrary, he considered it appropriate to assume that the company would continue to have this

support. He concluded, therefore, that it would be artificial to focus on working capital to determine solvency, particularly at a time when a company such as PPS, which does not have continuing work but rather has project work when required, is not actively engaged in a project. There is only a requirement to have recourse to working capital when a project is under way.

[61] Because Mr Petterson had expressed the view that at the material time PPS was insolvent, Mr Ruscoe gave evidence on the factors that must be established for that view to be formed. He noted the absence of most of those factors and concluded that to form the view that the company was insolvent Mr Petterson must have taken into account the claim by McDow as a due debt. Mr Ruscoe's view is that the sum claimed by McDow was not a due debt. On the information made available he formed the view that the company had sufficient cash to pay whatever due debts it had, when the transactions under review were entered.

[62] For the reasons I have already given, the sum claimed by McDow was not a due debt. I therefore accept the evidence of Mr Ruscoe. At the time the transactions were entered, PPS was solvent as defined in s 4 and able to pay its due debts, a position, which on the information available to the Court, appears to have prevailed for several years.

[63] Further, it had substantial cash reserves. They were sufficient to repay the entire sum of $1,253,537 which was paid to Mr Browne, DBC and DBM on 2 September 2008, without any further advance at that time by Mr Browne. Therefore, I accept that the advance he made was for the purposes of operating the company, not to repay the previous advances. This is a material difference from a "money-go-round" case such as *Re Manson & James Ltd*.[10]

[64] In that case the company granted to a director a debenture to secure an advance of $20,000. The director advanced that sum to the company, and it immediately repaid to him an unsecured advance of $19,950. The Court found there was no material advantage to the company, and the substance of the transaction was

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[10] *Re Manson & James Ltd (in liq)*, above n 7.

to give the director priority for his debts over other extensive creditors. But for the second advance, the unsecured advances could not have been repaid.

[65] It is quite lawful, and indeed commonplace, for private companies to receive advances from shareholders and related companies as their requirements for cash fluctuate, rather than retaining their own funds which are not required all the time, or borrowing from an external lender such as a bank. It appears that PPS had habitually been funded as required by its bankers, or by shareholder or related company advances, or both.

[66] Mr Ruscoe also said that it is his advice, in this circumstance, to those advancing funds to the company to take security and, again, for companies in the position I have described, this is both lawful and beyond criticism, unless there are further circumstances which direct that the granting of a charge, which might otherwise be beyond reproach, should not have occurred.

[67] The second element of context is the restructuring of the affairs of Mr and Mrs Browne, their family trust and the companies in the group. Evidence was given about this by Mr Browne, and he was cross-examined on it. Mr Gustafson analysed this evidence. His position is that Mr Browne's evidence is contradictory and unreliable. I will examine it shortly. However, he did not refer in his submissions to the evidence of Mr J R K Wolt, nor was Mr Wolt called for cross-examination on his affidavit.

[68] Mr Wolt is a financial advisor. He is a director of the firm which provides financial advice to Mr Browne and his wife. He has personally acted for Mr Browne since 2000. Mr Wolt says that Mr and Mrs Browne had been involved in restructuring their financial affairs over a period predating the transactions in issue in this case. This was being undertaken because of a need for long term estate and succession planning and, in particular, five factors. The first was Mr Browne's age and a decision he made to pull back from his involvement in the various businesses operated by the group of companies in order to spend more time pursuing personal activities.

[69] Secondly, Mr and Mrs Browne have two sons and wished to involve them more in the business. Mr Browne had shown increasing confidence in his sons taking over management and governance roles, particularly in the context of the investment by Frank GmbH (with which Mr Browne has had a close personal working relationship for many years) in PKS Frank.

[70] Thirdly, Mr and Mrs Browne's sons wished to have their own company or business within the group, and they had a focus on the high density polyethylene pipe manufacturing and supply side of the business.

[71] Fourthly, Mr Browne is an active investor. He has developed the group company structure over many years by identifying opportunities and continually expanding into new areas. Use of institutional financing has been limited, and heavy reliance has been placed on inter-company advances and funding through the Browne Family Trust. This has resulted in Mr and Mrs Browne's assets being tied up in the company structure.

[72] Fifthly, Mr Wolt has advised Mr and Mrs Browne for a number of years that they should reduce their investments in their companies in order to diversify their investments and increase liquidity both personally and in the family trust. Mr Wolt says this is of particular significance for Mrs Browne because if anything were to happen to Mr Browne, it is important that she has access to cash and liquid investments to ensure her lifestyle is not compromised. Within the existing company structure that was not the case.

[73] Therefore, the advice given by Mr Wolt has been aimed at ensuring that Mr and Mrs Browne improve their own personal liquidity by withdrawing investments from the group structure. Mr Wolt says this cannot be achieved promptly, and withdrawal must be over a period of time and when opportunities are available.

[74] As a result, restructuring of the group has developed over a number of years, and the estate and succession aspects of the restructuring predate the transactions in issue. The restructuring also requires ongoing management and adjustment because

the group does not remain static and continues a process of acquisition, expansion and divestment.

[75] On the transactions in issue, Mr Wolt says:

> The PPS restructure was part of the estate and succession planning I have referred to. It was one of the companies where Mr Browne wanted to reduce his involvement, both financially and time wise. It was a company that was identified as being well suited for Mr Browne's sons to step up and take a more active role.
>
> The repayment of Mr Browne's current account and the repayment of the intercompany advances from David Browne Mechanical and David Browne Contractors Ltd were discussed with me as part of the restructuring process that I have referred to and formed part of my advice.
>
> I was aware of some wider issues affecting PPS, including problems with a former employee who had set up in competition, the claim by McConnell Dow Constructors Ltd and reservations of the German investors in light of those matters. I am also aware that Mr Browne's sons expressed a preference to form a new company against the background of these matters and that this was a preferred option for the German investors.
>
> The decision of Mr Browne's sons decided (sic) to start a new company did not alter my advice to Mr Browne to take the opportunity to withdraw his investments, and those of the associated companies, from PPS.

[76] Mr Browne gave evidence which supports Mr Wolt's description of the reorganisation of the affairs of the group of companies and, in particular, PPS. He says that he had reached a stage in his life where he wanted to reduce his involvement in that company and other companies in the group, and to give two of his sons an opportunity to set up and take a more active role in the management of the group of companies. This involved a wider restructuring of his financial affairs which included withdrawing his investments in the form of loans to PPS and dealing with the shares in PKS Frank NZ Limited, which were held by PPS. He says that Mr Wolt was the personal financial advisor that he and his wife used, and Mr Wolt had been advocating that they begin a staged withdrawal of their investments from various companies in the group.

[77] Mr Browne says that at the time PPS was having difficult issues with a former employee, Mr Begg. He had left the company after many years service and set up in opposition. This had caused friction with Frank GmbH Limited which was an investor in PPS Frank NZ Limited. It was therefore necessary to look at setting

up a new company to take over the operations of PPS if the support of Frank GmbH, and its ongoing investment, was to be maintained.

[78] As well, Mr Browne's sons had reservations about the effect on the reputation of PPS of the McDow claim and Mr Begg's actions. Although Mr Browne had anticipated that his sons would take over the PPS business, their expressed preference was to set up a new company, and as a result Frank PKS Limited was set up in December 2008, with the Browne Family Trust, Frank GmbH and Mr Browne's two sons as shareholders.

[79] Mr Browne says that the McDow claim was also a factor under consideration in the restructuring of PPS, but not because he accepted that PPS had any liability to McDow. The most significant effect of the McDow claim on the decision-making process was the impact it was having on the confidence of Frank GmbH and its willingness to continue investing in PKS Frank.

[80] All these reasons led to the decision which resulted in the investments Mr Browne, DBC and DBM had in PPS being withdrawn, but to his agreeing to fund the continued operation of the company to the extent necessary. The decision to do this as a secured lender was on the advice of the company's solicitors. PPS itself would be wound down.

[81] In cross-examination, Mr Browne was asked about whether PPS was in fact being wound down. Mr Browne said that at about the same time as the transactions in question, he was in discussions with McDow over the possibility of a comparatively major contract with McDow for a pipeline in Albany. Although no contract had been entered, the indication from McDow was that PPS would be given a contract. If that occurred, it would be necessary to buy further plant for the project and this was the reason he put further funding back into the company. In the event, PPS was awarded the contract.

[82] It was put to Mr Browne that this was inconsistent with the notion that PPS was being wound down. His response was that it was not being wound down but was being restructured in order to change the nature of his investments, and for him

to step away from the day-to-day running of the business. This, Mr Browne said, applied to all the companies in the group, which were under review and it was not just PPS which was being restructured. He gave other examples. I return to this after reviewing the evidence of Mr Lay on this point.

[83] Mr Lay, a chartered accountant who acted for PPS, also gave evidence in relation to the restructuring. He said its purpose was to wind down the company's operation. The company had cash reserves and few, if any, creditors so restructuring was straightforward. The long term plan was to wind down the operation of PPS. The agreement reached was that the advances from Mr Browne, DBC and DBM would be repaid, which PPS was able to do from its cash reserves.

[84] It would also be necessary for the company to have access to further monies to continue operations when needed and Mr Browne had cash which he was prepared to advance. This option was taken, rather than continuing with a bank facility. The bank security over the company was therefore discharged.

[85] Mr Lay envisaged that PPS would eventually be wound up. It was calculated that $450,000 should be a sufficient sum to fund its ongoing operations until that occurred, so that was the sum which Mr Browne advanced to the company.

[86] Mr Lay accepted that when the transactions in issue were under discussion there were also discussions about the McDow claim and that if it succeeded, it would be for a substantial sum.

[87] From this evidence I make the following findings. First, prior to, and throughout the period in question, there was ongoing activity involving not just PPS but other companies in the group by way of restructuring. The reasons for this are those which are set out in the unchallenged evidence of Mr Wolt. The evidence of Mr Browne and Mr Lay is consistent with that. I am satisfied that the transactions involving PPS were not one off transactions, and they were undertaken for several reasons including the difficulties being experienced with Mr Begg, the concerns Frank GmbH had and its wish to be distanced from the problems with McDow, Mr Browne's wish to bring his sons into the business, coupled with their wish to do

so, but in a separate entity (which tied in with the position of Frank GmbH) because of the stigma attached to PPS as a result of the McDow claim.

[88] The evidence of Mr Browne and Mr Lay differs in relation to PPS in one material respect, but I have concluded that the difference is readily reconciled. Mr Browne said in his affidavit that for the reasons I have referred to, PPS was to be wound down. In cross-examination he maintained that PPS was not being wound down; Mr Lay maintains it was. After considering the evidence given by each of them, both in their affidavits and under cross-examination, I have concluded that these differences are more apparent than real. When Mr Browne spoke of PPS not being wound down, I am satisfied that he was speaking of the business of PPS, because he talked about this in the context of the possible Albany contract. In other parts of his evidence he talked about there being a new company run by his sons which would take over the operations of PPS. The conclusion I have reached is that it was always intended that the business of PPS would continue, and that it would be PPS which carried it on for an unspecified period while decisions were made about how the business would be carried forward. This, in turn, depended on the wishes of Mr Browne's sons, and the wishes of Frank GmbH. If a new company was formed, the activities of PPS would be wound down. In the event, a new company was formed in December 2008 with Mr Browne's sons as directors.

[89] I find, therefore, that there is no material inconsistency in the evidence on this point; rather, the evidence is consistent with the goals described by Mr Wolt, to hand over control of the business to Mr Browne's sons, for Mr Browne to take a less active role in the day-to-day operation of the business, and for the funding which the family had in PPS to be withdrawn for the reasons he expressed.

[90] It is also consistent with the position that PPS was in at the time, with one significant contract pending, for Mr Browne to keep funding the operation of PPS until steps were taken to effect the final stages of the restructure. Significant criticism was levelled on behalf of Mr Petterson at the fact that Mr Browne advanced monies to PPS at a time when it did not in fact need cash. However, Mr Browne clearly had an eye on the Albany contract, and the need for funds to be in the company if that contract was awarded. He also had Mr Lay's calculation of the sum

that would be required to run the company until the restructure was complete, and he advanced the sum Mr Lay had calculated. I do not find the criticism justified. If Mr Petterson wished to substantiate this criticism he could have presented a cashflow for PPS from September 2008 to March 2009, if that would have supported his view. As it was, Mr Gustafson looked only at the date of the advance, but that is unrealistic, particularly in the case of a company which carried out project work as it arose.

[91] The third element of the circumstances in which the transactions were entered is the two claims which had been made by McDow at that time. Although PPS was solvent, paying all creditors when due, and supported financially, when necessary, by its shareholders and related companies as well as its bankers, it had one major issue on its plate: a substantial claim for damages, larger than its net worth. Mr Browne, and therefore DBC and DBM, say they strongly believed the work of PPS was not the cause of failure of the pipe but, even if it was, their work was covered by McDow's insurance. Therefore, they proceeded with the transactions in question, which were part of a much larger restructuring plan which was underway.

[92] Mr Gustafson, however, characterises the actions of Mr Browne, DBC and DBM as a deliberate course of conduct embarked upon to ensure that sums they had advanced were repaid and any further advances by Mr Browne were secured so as to take priority over other creditors. They knew, or strongly suspected, this would include McDow. Indeed, creditors almost entirely consisted of the sum claimed by McDow and they knew this claim would almost certainly succeed and that they were not insured.

[93] Mr Browne's response, and that of PPS, to the McDow claim must now be examined. As I have said, Mr Browne maintains that the only relevance of the McDow claim to the decisions which led to the transactions under review was the effect the claim was having on the reputation of PPS and on Frank GmbH, and its relationship with PPS. That, the difficulties with Mr Begg, and the family asset restructuring, were three of the reasons Mr Browne had for shifting the business of PPS from PPS to a new entity. His evidence is that from receipt of the first claim onwards, he believed the allegations of faulty workmanship on the part of PPS were

unfounded, that the company had no liability to McDow whatsoever, and that McDow was insured for the losses arising from the events which had occurred. He believed the failures in the joints of the pipes were caused by the way they were handled, a procedure which he criticised before it was actioned. He believed that the method PPS employed to join the piping sections and to check their work as they proceeded with the construction process was such that there were no faults in the welding. Any faults that there might have been would have been eliminated at the time the work was done. He described the process of constructing the pipe lengths to support this contention.

[94] Mr Petterson's case, however, is that PPS knew that there was a substantial risk that it would be found liable for the failures of the pipe, that it took few, if any, steps towards endeavouring to prove that it was not liable, that although it thought McDow was insured, it did not take legal advice until November 2008 on whether this was the case, and that it repaid the shareholder and related company advances and granted a security to Mr Browne for any future advances because it knew it could not meet the McDow claims and that it would almost certainly be liable to do so. With the particular knowledge it had of the strength of the McDow claims, it took active steps to prefer DBC , DBM and Mr Browne over unsecured creditors by paying out their advances and giving a security to Mr Browne for any further advances he made.

[95] I refer first to the evidence on PPS taking legal advice on the claim. Mr Browne was asked about a letter PPS received from its solicitors, dated 17 November 2008. The letter dealt with evidentiary issues concerning liability for the pipe joint failures, as well as with insurance. PPS was advised of categories of expert advice which would be required in order to determine whether PPS was liable for faulty workmanship, or whether McDow was liable for the broken joints because of the way the pipe was handled once constructed into long sections. The solicitors noted that PPS had engaged Frank GmbH to report in relation to the method used by McDow to hold the pipe on the seabed, but recommended the engagement of an independent expert because of the association between PPS and Frank GmbH. They also recommended that a quantity surveyor be engaged to advise on the quantum of the claims which had been received.

[96] Mr Gustafson put to Mr Browne that this was the first time that PPS had obtained legal advice about liability for the claims, a proposition he denied. He said there had been a lot of discussions prior to this letter, but this was the first written advice. PPS had also taken advice on the installation procedure from Frank GmbH, as well as from a university in Spain.

[97] Next I refer to the evidence of Mr Browne on the strength of the claim. In cross-examination he was questioned on an email received from Dr Habedank of Frank GmbH on 14 July 2008. The email says:

> It is clear for everyone involved that the problems occurred during the installation of the Christchurch outfall were caused due to faulty weldings. This was confirmed during our last shareholder meeting.
>
> As agreed during our telephone conversation (David B) I kindly ask you to consult a lawyer and to write an official letter to MacDow that responsible for these problems is PPS. They also performed the welding in the production and were paid for it by MacDow. The pipe has in no point be claimed and all quality controls etc. were performed.
>
> Furthermore, we have tested some welding samples from PPS here in Germany with very bad results. We asked Daniel to forward the used welding parameters and got no feedback.

This email was not produced by its author. It seems it was found among the records of PPS.

[98] It was put to Mr Browne that this was expert advice from Frank GmbH, which has expertise in this area, on PPS's liability for the failure of the welds. Mr Browne denied this. The email was written in response to a letter from McDow to PPS Frank holding PPS Frank liable for the welding. McDow evidently took the view at that point that, as the construction of the pipe sections was undertaken at PPS Frank's workshop, PPS Frank must be responsible for it. Mr Browne says that in his view, Dr Habedank's email was sent to explain that it was not PPS Frank which did the welding, it was PPS. PPS acted on the email by telling McDow that PPS Frank had not undertaken the welding, it had only manufactured the pipe. The welding was undertaken in the workshop of PPS Frank, but not by PPS Frank.

[99] When asked further about the statement that the problems which occurred in the installation of the pipeline were caused by faulty weldings, Mr Browne first

explained the system for welding which is undertaken. It involves welding pipe sections together sequentially by a specific procedure with every tenth weld being tested. In the event of a failure, the previous weld is tested so as to ensure that the procedure for welding was correct and effective. This led PPS to believe that the failure of the pipe was not caused by the welding. Mr Browne said that a joint can only be tested by destruction and that the weld which had failed has not been tested since the failure. All that has occurred is that experts have viewed it, and McDow has refused to give it to PPS to test, or to send it to Germany for testing.

[100] In relation to the paragraph in the email which refers to testing welding samples from PPS with very bad results, it was suggested to Mr Browne that this must have given him concern about the liability of PPS on the McDow claim.

[101] Mr Browne said that pipes as thick as these ones had never been welded before. The process which is undertaken is to put pressure on the end plates of the pipes with heat and allow the heat to soak into the polyethylene so it fuses. It took some eight months to perfect the welding technique given the extraordinary thickness of the material. Eventually the correct parameters for welding this material were established and test welds were satisfactory. As I understand Mr Browne's evidence, he believes the reference in the email to test welds was to welds undertaken during the process of establishing the parameters to be used, not while the long pipe sections were being welded together. He also pointed out that Frank GmbH is a pipe manufacturer, not an expert on pipe welding. Mr Browne accepted, however, that he was concerned about the failure of the welds referred to in the email; as he put it, "You've got to have some concern that things aren't right."

[102] I accept Mr Browne's explanation that McDow had claimed that PPS Frank was responsible for the welding failures and that part of the email records that PPS Frank was not responsible because it did not in fact perform the welding in question. That was done by PPS. Further, there could be no suggestion that the pipe product itself was faulty.

[103] I also accept that the welding samples which were found to have very bad results were not samples of welding undertaken during the course of manufacture of

the pipeline, and that in fact the failed pipeline joints have never been made available to PPS, or for that matter Frank GmbH, to test. I accept Mr Browne's evidence that joints are progressively tested during the sequential construction of smaller lengths of pipe into longer sections. There was no contrary evidence on these points. Dr Habedank was not called to give evidence. There is no other reason to doubt Mr Browne's evidence.

[104] However, the passage in the email which might be most adverse to the position of Mr Brown, is the sentence "It is clear for everyone involved that the problems occurred during the installation of the Christchurch outfall were caused due to faulty weldings. This was confirmed during our last shareholder meeting." On the face of it, that suggests acceptance of liability for faulty welding, but it is unclear who might have given that acceptance. The phrase "everyone involved" is, at best, vague. Reference to the shareholder meeting suggests it may have been a group including Mr Browne and Dr Habedank, but that is not established.

[105] In my opinion, the most that can be taken from the email is that at the time of the shareholders' meeting referred to, which was presumably shortly before the date of the email, and when the email was received, there was doubt on the part of PPS on whether Mr Browne's conviction that PPS was not liable would turn out to be correct. But I am unable to draw more from the email in the absence of its author, or any further details of the circumstances in which it was sent, or who is referred to in it. I am mindful that the email comes from Frank GmbH and shows that company distancing itself from responsibility.

[106] Having said that, however, other facts also bear on whether Mr Browne could reasonably have held this view on liability. First, the eight month process by which PPS developed the correct protocol for welding together sections of pipe of a dimension which had not been welded before, appears to have led to a welding process which was successful. Although three joints failed, hundreds did not.

[107] Secondly, from the outset, PPS had grave concerns, which it expressed to McDow, about the way the pipe was being handled. This was not just in relation to the way it was placed and anchored on the seabed, it also covered the way the pipe

was handled in transit, a procedure which evidently bent the pipe thereby putting unexpected strain on the joints. Although this process is said to have changed at some point, this issue was not examined in any detail in evidence. In particular, there was no evidence that any different handling technique which may have been used was any more or less likely to have caused damage.

[108] Thirdly, McDow had not made available to PPS the failed joints for testing.

[109] Fourthly, as Mr Browne said, PPS itself is an expert in this field and whilst not able to bring an independent view to bear, due weight must be given to its expertise.

[110] I conclude, therefore, that whilst, at the relevant time, two joints had failed and there had been some expressions of opinion of persons, who cannot be identified with certainty, that welding failure caused the joint failure, there were also sound reasons for Mr Browne to hold a contrary view.

[111] Also, by July and August 2008, the basis for the claim by McDow does not seem to have been substantiated by the provision, for example, of its own expert reports. Liability had been levelled at PPS and the claim in respect of the first pipe failure had been quantified. There is no evidence, however, that any expert reports supporting McDow's contention that failings on the part of PPS were the cause of the joint failures, had been provided to PPS. Overall, therefore, whilst there was reason for some concern on the part of PPS, and indeed Mr Browne accepted that he had a level of concern, I am not satisfied that the McDow claim had been presented to PPS with an evidentiary foundation when PPS entered the transactions under review.

[112] Ultimately, of course, McDow did present expert evidence, as did PPS, and the McDow claim prevailed at an independent adjudication. That was not until eleven months later.

[113] As I have noted, Mr Browne also believed that there was insurance cover in place which would pay the greater part of the loss incurred by McDow. He accepted

that PPS would need to repair the welds which failed if it was found that the failures were due to its faulty workmanship. He said, however, that at all times he believed (and still believes) that McDow had insurance which would pay the additional expense of recovering the pipe from the seabed and re-laying it after repair.

[114] Mr Gustafson strongly challenged this view, maintaining that Mr Browne had no basis for believing there was insurance in place and that PPS had not in fact taken legal advice on this point at the time the transactions were undertaken. In fact, when legal advice was obtained in November 2008, it was to the effect that no cover was held.

[115] Mr Browne said, however, that the question of insurance cover was fully discussed with McDow prior to the contract being entered and that McDow made it clear that it was carrying insurance, so PPS need not do so. Mr Browne says he was careful to check this because it differed from the situation which had applied n previous contracts with McDow and he would not have entered the contract had there not been insurance in place. He referred to having undertaken sewer outfall jobs for McDow in Fiji and in Dunedin, and another pipeline for McDow on an installation for Fonterra at an unspecified location. No contrary evidence was given.

[116] Mr Browne took advice from its insurance broker, McLaren Young International, when the claim was made. It was advised that the policy McDow held would respond to the losses it had incurred. This advice was given in writing on 18 April 2008 and was produced in evidence. The chartered loss adjuster who gave this advice was not called. His view was not contradicted.

[117] Mr Browne also said that in November 2008, when PPS's solicitors advised that the policy would not respond to the loss which had been incurred, he was faced with opposing advice and preferred the advice of the insurance broker as an expert in the field.

[118] Questioning of Mr Browne by Mr Gustafson seemed to proceed on the basis that McDow did not hold insurance cover for the events which occurred. It did, however, have an insurance policy, but the evidence in relation to the extent of the

cover available under the policy held by McDow is inconclusive. There is evidence to suggest that the policy would in fact respond to the McDow losses, but McDow would incur an excess and also lose a no claims discount. There is evidence that McDow in fact claimed, but faced with these facts withdrew its claim. There is no evidence on why the liquidator has not pursued a claim under the policy. There is a suggestion for PPS that the liquidator has preferred to bring a claim against PPS because, if that were successful, McDow would recover most of its loss, whereas if the insurance policy responded, McDow would only do so at the cost of the excess and the lost discount.

[119] In the end, none of these points was substantiated. There is sufficient evidence before the Court to give a level of concern that Mr Petterson has not thoroughly investigated whether there is insurance cover for the losses, but in the present context that is not relevant. The case for the liquidator in relation to insurance is that, when the transactions were entered, PPS had no sufficient reason to believe that it had insurance cover, so it had no proper basis for relying on there being cover as a reason to proceed with the transactions in the face of the claim.

[120] I find that this is not made out. It was not until three months after the transactions that formal advice was given by the solicitors for PPS on cover under the policy. At all times prior to that, the advice PPS had sought and obtained was to the opposite effect. That advice was in accordance with the advice McDow had given to PPS in relation to insurance cover prior to the contract being entered. The evidence on that point is not challenged: Mr Petterson did not lead evidence from anyone from McDow.

[121] Mr Gustafson also questioned whether McLaren Young International had the full details of the policy at the time it gave the advice PPS relied on. He attempted to piece this together by reference to various documents, but did not introduce evidence from the loss adjuster, who would have been able to say. Mr Browne was questioned on it, but it is difficult for him to know what the adjuster had in front of him. The fact is that the advice was given, it appears on its face to be soundly reasoned, and the evidence does not satisfy me that there is any reason to doubt that, when it was given, it was properly considered advice of the broker.

[122] A belief that the McDow insurance policy would respond to McDow's losses might legitimately have coloured PPS's response to the claim. PPS had, as I have found, sound reason to believe that its liability would only be the cost of repairing the welds, not the very substantial costs of recovering and relaying the pipe, those being covered by insurance. In this circumstance, even if it were established that it was slow to seek evidence and take advice on its liability, as Mr Petterson maintains, that could be more readily understood.

[123] The belief is also relevant to the fact that, at the directors' meeting where the resolutions were passed which authorised the transactions under review as well as other meetings, the McDow claim was discussed and, as Mr Lay accepted, it was realised that if it succeeded it would be substantial. But, PPS had been advised that there was insurance cover for the claim and the directors, of whom Mr Browne was one, were entitled to take that into account when making their decision on the transactions under review.

[124] Mr Gustafson criticised the evidence presented by Mr Browne in a number of respects. He said that in his affidavit Mr Browne maintained that he had had legal advice that there was insurance cover, but there was no proof that legal advice had been given. In cross-examination on this point, Mr Browne referred to advice having been given by another firm of solicitors.

[125] I think Mr Gustafson's point is well founded. The evidence points to the advice from PPS's solicitors being given in November. Prior to that the advice had been from PPS's loss adjuster. If there was other legal advice prior to that, it was not produced or described in any detail. It seems Mr Browne was probably wrong on this point, but that does not change the fact that he had sought and obtained advice from PPS's loss adjuster. Nor, taking into account the totality of his evidence, does it reflect adversely on his credibility to any material degree.

[126] Mr Gustafson also criticised PPS for not making bank statements available to the liquidator. This was partly in response to criticism of the liquidator for waiting so long after the commencement of the liquidation to take steps to challenge the transactions in issue, and partly to show that PPS was reluctant to have the

transactions opened up to scrutiny. There is an email from PPS's solicitors which, on one interpretation, could suggest deliberate withholding of bank statements. However, the author of the letter was not called, nor was its context established, and I therefore find it unhelpful. Mr Browne was criticised personally for not handing over records, but his response was that he had given them to the receiver, Mr Stavely. Documents show that Mr Stavely responded promptly by providing to the liquidator information he sought. The evidence or these issues added nothing to the strength of Mr Petterson's claim.

[127] Mr Gustafson placed some reliance on a letter sent to the directors of PPS by its solicitors on 27 May 2009. It contains the following passage:

> From an overall position I think we have effectively now achieved what we set out to do some 9-10 months ago to
>
> - Look to wind down in an orderly manner Polyethylene Pipe Systems Limited; and
>
> - Extract out the wealth and cash in the company in an orderly and legal manner; and
>
> - Ensure that the stakeholders in the company are paid in the ordinary course of business, and particularly ensure that you, either via your current account or your secured advance, are paid out in the normal course of business.

[128] Mr Gustafson relies on this letter to bolster his contention that the directors of PPS embarked on a deliberate course of action to strip out cash from PPS by undertaking the transactions under review. In the overall context of the case, however, I am not satisfied that this letter supports this contention. When read against the uncontested evidence of Mr Wolt on the overall restructuring of the Browne family interests, and the evidence on the reasons given for changing the way PPS operates, the letter goes no further than recording that the intended steps had been achieved. Again, its author was not called to give evidence or to be cross-examined on whether the letter was in fact intended to bear the meaning for which Mr Gustafson contends.

[129] Finally, Mr Gustafson criticised the sale by PPS of shares it held in PKS Frank. He aimed his criticism at the fact that the transaction took place at the amount of a valuation by Mr Lay, suggesting, as I understand it, that the valuation

should not have been relied on. However, he did not lead any evidence to suggest the valuation was incorrect, so this point was entirely without substance. Put simply, if the valuation was accurate, it does not matter who formulated it.

Conclusion on whether it is just and equitable that the charge in favour of Mr Browne be set aside

[130] I have concluded that when the charge was given, Mr Browne and PPS had sound reasons to believe that the failure of the joints was not caused by faulty workmanship undertaken by PPS. Furthermore, at that time they had sought, received and justifiably relied on advice that the insurance policy held by McDow would give that company cover for the losses it had incurred (apart from the actual cost of rewelding the joints which would only be the responsibility of PPS if it was later established that its welding had been faulty). The transactions in issue were undertaken by a company in sound financial heart, and were part of ongoing re-arrangement of the affairs of companies in the ownership of the Browne family which had commenced well beforehand and were for legitimate reasons. The substance of the transaction was to effect a legitimate re-arrangement of the finances of PPS in circumstances where that was acceptable conduct.

[131] The fundamental basis for Mr Petterson's case under s 299, that it is just and equitable that the charge given by PPS in favour of Mr Browne be set aside, is not made out.

[132] Given the findings I have recorded it is not necessary to consider the remaining issues arising on this proceeding.

Orders

[133] On the strength of these findings, I make the following orders:

(a) The application to set aside the charge under s 293 is dismissed.

(b) The application to set aside the charge under s 299 is dismissed.

[134] Costs are referred to below.

Claim 900 against David Browne Contractors Limited and David Browne Mechanical Limited

[135] As I have recorded, the notices issued by Mr Petterson against DBC and DBM expired without either company having given written notice of objection under s 294(3) of the Companies Act 1993. In this circumstance, each payment was automatically set aside under that same subsection.

[136] For the reasons I have also recorded, both of these notices, and the notice issued against Mr Browne, were flawed.[11] Had notices of objection been given, the notices by Mr Petterson would have been set aside. He now relies, however, on the fact that each transaction is automatically set aside to seek repayment orders under s 295 of the Companies Act.

Under s 295, is there a discretion to make an order, or not?

[137] Section 295 provides, to the extent relevant:

> **295 Other orders**
>
> If a transaction or charge is set aside under section 294, the Court may make 1 or more of the following orders:
>
> (a) an order that a person pay to the company an amount equal to some or all of the money that the company has paid under the transaction:

[138] Mr Gustafson submits that once an insolvent transaction has been established by the procedure set out in s 294, there is no discretion in relation to whether an order should be made, or not. His argument is based on the proposition that authorities in Australia on materially identical provisions have established that there is no discretion.

[139] In *Cashflow Finance Pty Ltd v Westpac Banking Corporation*, a decision of the Supreme Court of New South Wales Equity Division Commercial List, Einstein J said:[12]

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[11] [23] – [30] above

[12] *Cashflow Finance Pty Ltd v Westpac Banking Corporation* [1999] NSWSC 671 at [569].

(ii) The jurisdiction that is conferred by s588FF(1) is to make 'one or more of the following orders'. There is, I accept, clearly a choice to be made by the Court as to which of the orders in the list ... is appropriate to be made. That does not mean that, once the Court is satisfied that the circumstances exist which make it appropriate for a preference or uncommercial transaction to be set aside, there is then some separate discretion which the Court can exercise on the 'palm tree justice' grounds, in deciding whether to actually make the order.

(iii) The power conferred by s588FF is one where:[13]

> The word 'may' is merely used to confer the authority: and the authority must be exercised, if the circumstances are such as to call for its exercise.

[140] This case was applied in *Cussen v Saltan*,[14] and *Frontier Architects Pty Ltd (In Liq)*.[15]

[141] However, these cases have not been applied in New Zealand. Recognising this, Mr Gustafson submits that in *Allied Concrete Ltd v Meltzer & Ors*,[16] the Supreme Court has taken the approach of Australian authorities to interpretation of s 296(3)(c) of the Companies Act, and the same should be the case with s 295.

[142] In *Levin v Timberworld Ltd*, the Court accepted that there is a discretion under s 295.[17] Associate Judge Abbott said:

> [73] Section 295 states that the Court "may" make one or more of the orders set out in the section, including those set out in s 295(a) and (c). The section does not state how that discretion is to be exercised, and it is by no means certain that there is a general discretion once an insolvent transaction has been established.

For the latter proposition, the Judge cited Heath and Whale on Insolvency[18] and *Cussen v Saltan* above.

[143] His honour then referred to *Levin v Market Square Trust*,[19] to which I refer below, and continued:[20]

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13 *Finance Facilities Pty Ltd v Federal Commissioner of Taxation* (1971) 127 CLR 106 at 134-135.
14 *Cussen v Saltan* [2009] NSWSC 671 at 24-30.
15 *Frontier Architects Pty Ltd (In Liq)* [2010] FAC 1381 at 26-28.
16 *Allied Concrete Ltd v Meltzer & Ors* [2015] NZSC 7.
17 *Levin v Timberworld Ltd* [2013] NZHC 3180.
18 Heath and Whale, above n 4, at [24.119].
19 *Levin v Market Square Trust* [2007] NZCA 135, [2007] 3 NZLR 591.
20 *Levin v Timberworld Ltd*, above n 17.

> [75] Reading s 295 in relation to these authorities it seems that the Court has a discretion not to order payment if to do so would cause unfairness to the creditor. However, given that Parliament has prescribed in s 296(3) particular conditions under which a payment must not be set aside on the basis of unfairness to [a creditor], the threshold for any further discretion under s 295 should be a high one, going beyond a general sense of unfairness to some cogent and compelling factor going beyond the s 296(3) defence. Anything less would undermine the requirements of s 296(3) and would also be an unprincipled departure from the basic principle of the insolvency regime to achieve fairness amongst all creditors (inter se) as distinct from doing justice or achieving fairness between a particular creditor and the company.

[144] In *Levin v Market Square Trust*, the Court of Appeal said:[21]

> Considerations of fairness (using that concept loosely) arise later in the regime, when the court is considering what orders, if any, to make under s 295 or whether to deny the liquidator recovery under s 296(3).

[145] Plainly the Court of Appeal considered that there is a discretion given by s 295 on whether to make any order at all, and that this is separate from the decision required under s 296(3).

[146] In *Farrell v Fences & Kerbs Ltd*, the Court of Appeal said:[22]

> If the creditor does not establish an entitlement to protection under s 296(3), a discretion remains under s 295 as to the extent to which the creditor must repay the payment or other property or benefits received.

[147] This position is reflected, also, in *Grant v Lotus Gardens Ltd*.[23] As part of a discussion of s 295 and s 296(3), the Court of Appeal found that s 295 is not an exclusive pathway for a liquidator to obtain an order following a setting aside of a payment or security. Existing common law and equitable remedies still apply. The Court then said:[24]

> [38] Moreover, s 295 does not use exclusive or mandatory language. It states that the Court "may" make the orders set out in that section, and contains no words excluding any other remedy. There is no doubt that s 295 gives flexible discretionary powers to a liquidator.

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21 At [49].
22 *Farrell v Fences & Kerbs Ltd* [2013] NZCA 329 at [3].
23 *Grant v Lotus Gardens Ltd* [2014] NZCA 127, [2014] 2 NZLR 726.
24 At [38].

This passage does not expressly deal with the question of whether the Court may elect not to make any order at all, but it demonstrates an approach consistent with that position.

[148] In *McKinnon v Falla Holdings Ltd* the Court also recognised the existence of a discretion – see [151] below.

[149] The law in New Zealand, therefore, differs from the law in Australia, as matters stand, in relation to the discretion given by s 295. This Court is bound by the Court of Appeal. Decisions of the High Court are persuasive. I am not prepared to apply the Australian approach in the face of the New Zealand authorities.

[150] I therefore proceed on the basis that there is a discretion on whether to make any order under s 295, whilst noting the view expressed in *Levin v Timberworld Ltd*, which Mr Russ submits is the correct approach for consideration of the discretion.

[151] It is established that if a transaction is set aside under s 294, then on a subsequent application under s 295 for recovery by a liquidator, the recipient of the funds which the liquidator seeks to recover cannot argue that the transaction was not voidable. Arguments to that effect could and should have been raised on an application under s 294. The authority for this principle is *McKinnon v Falla Holdings NZ Ltd (in liq)*.[25]

[152] Notwithstanding this, setting aside does not lead inevitably to a recovery order in favour of a liquidator. As Chambers J recognised:[26]

> First, the remedies available under s 295 are discretionary. Secondly, even if the Court decides to make one or other of the orders, it is clear from the wording of s 295 that recovery may not be total. Thirdly, s 296(3) confers a wide discretion on the Court to deny recovery in certain circumstances.

[153] In one of the cases referred to by Chambers J, *Huberg Distributors Ltd (in vol liq) v Harvest Foods (NZ) Ltd*, Tipping J said:[27]

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25 *McKinnon v Falla Holdings NZ Ltd (in liq)* (1999) 8 NZCLC 262,034.
26 *McKinnon v Falla Holdings NZ Ltd (in liq)*, above n 25, at 262.041.
27 *Re Huberg Distributors Ltd (in vol liq) (No 2)* (1987) 3 NZCLC 100,211 at 100,215.

> In this case, as I have said, the liquidator has candidly and properly acknowledged that if he had known what he now knows he would not have sought to set aside the dispositions presently before the Court in the first place. That acknowledgement does not in my view lead to the proposition that the statutory setting aside should ipso facto be regarded as invalid but the point is highly material to the second aspect of sec 311A, namely recovery.

[154] His Honour went on to record that counsel for the liquidator indicated that he could not make any concession, in view of the liquidator's duties as a whole, but did not feel able to address any substantial argument against the proposition that if the dispositions were not voidable in the first place as a matter of fact, it would be inequitable to order recovery in full. Counsel for the creditor contended that it would be quite wrong and inequitable for the Court to order any form of recovery given that the liquidator accepted that the dispositions were not in fact voidable. His Honour then said:[28]

> While the Court would not wish to encourage those in the shoes of Harvest Foods simply to let time go by and then take a point such as this on an application for recovery, it does seem to me that as the liquidator was never entitled to avoid these dispositions it would be inequitable to order recovery, even though I am completely satisfied that the liquidator issued the notice under sec 311A bona fide and that as a consequence of Harvest Foods' inactivity the dispositions were statutorily set aside.

The Court declined to order recovery of the sum concerned.

[155] In the present case it is not possible to conclude that the liquidator takes a position, in relation to any of the transactions he sought to set aside under ss 292 and 293, akin to that taken by the liquidator in *Re Huberg Distributors*. Rather, and I mean no disrespect to the liquidator by this observation, I sensed from Mr Gustafson a slightly grudging acceptance of the proposition that the claim made by McDow at the time the transactions were entered did not constitute a due debt. That acceptance was, of course, sufficient for Mr Petterson to withdraw his claim against Mr Browne, but despite DBC and DBM having received notices based on a materially identical proposition, he vigorously pursued a claim for repayment.

[156] I do not think, however, that the approach of the liquidator to this issue in *Huberg Distributors* was the material factor governing the decision of Tipping J in

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[28] *Re Huberg Distributors Ltd (in vol liq)*, above n 27, at 100,215.

that case. His Honour's decision was based on the simple proposition that, as the liquidator was not entitled to avoid the dispositions in the first place, it would be inequitable to order recovery.

[157] The statutory provisions which apply to the transactions in question differ from those which applied when *Re Huberg Distributors* was decided. In *Meltzer & Mason v Fastlane Auto Ltd*, Associate Judge Abbott saw the discretion recognised by Tipping J in *Huberg Distributors* to be that which is now in s 296(3) of the Companies Act 1993.[29] This provides:[30]

> (3) A court must not order the recovery of property of a company (or its equivalent value) by a liquidator, whether under this Act, any other enactment, or in law or in equity, if the person from whom recovery is sought (**A**) proves that when A received the property –
>
> (a) A acted in good faith; and
>
> (b) a reasonable person in A's position would not have suspected, and A did not have reasonable grounds for suspecting, that the company was, or would become, insolvent; and
>
> (c) A gave value for the property or altered A's position in the reasonably held belief that the transfer of the property to A was valid and would not be set aside.

[158] Given the decision in the Court of Appeal in *Grant v Lotus Gardens Ltd*, I do not think that the only discretion available to the Court in relation to the making of an order under s 295 is contained in s 296(3).[31] Certainly, where a case falls within the circumstances in s 296(3) a recovery order cannot be made, but I do not see any reason why an order cannot be refused in circumstances akin to those before Tipping J in *Re Huberg Distributors*, as are those before the Court in the present case. I am firmly of the view that payment ought not to be ordered, for the very reason his Honour gave:[32]

> ... as the liquidator was never entitled to avoid these dispositions it would be inequitable to order recovery ...

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29 *Meltzer & Mason v Fastlane Auto Ltd* HC Auckland CIV-2005-404-3648, 20 September 2006.
30 Companies Act 1993, s 296(3).
31 *Grant v Lotus Gardens Ltd*, above n 23.
32 At n 27.

[159] For these reasons I decline to order DBC or DBM to repay any sum to Mr Petterson.

Outcome

[160] Both proceedings are dismissed.

[161] Costs are reserved. If not agreed, memoranda (not exceeding five pages in size 14 font) may be filed within 15 working days.

_____

J G Matthews
Associate Judge

Solicitors:
Kensington Swan, Auckland.
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