

## Legal update on insolvency law – December 2019

David Broadmore, David Perry, Jan Etwell, Kelly Paterson, Scott Abel, Scott Barker, Seb Bisley, Susan Rowe, Willie Palmer, Peter Niven, Myles O'Brien, Bridie McKinnon, Matthew Triggs, Oliver Gascoigne

11 December 2019

### Landmark decision on treatment of private information by liquidators

The High Court in *Henderson v Walker* [2019] NZHC 2184 found a liquidator, Mr Walker, liable for breach of confidence in relation to the distribution of part of Mr Henderson's private information, awarding \$5,000 in damages. The liquidator was also found liable for invasion of privacy in relation to distributions made to the Official Assignee, although no separate damages were awarded.

Mr Walker was appointed as liquidator of Property Ventures Ltd (and related group companies). He obtained access to a laptop and a tape drive on PVL's premises through search warrants issued by the Police during a period in which the liquidation itself was stayed. The laptop was used by Mr Henderson, the director of the company, and contained, among other things, personal and privileged information such as personal emails, family photographs as well as business emails.

In possession of that data, both during the stay of liquidation, and after that stay had been lifted, Mr Walker distributed it to various recipients, such as the IRD, the Official Assignee of Mr Henderson's bankruptcy, the Police and individuals that were argued to be hostile to Mr Henderson's interests.

Some of the key points that emerge from the Court's decision include:

- During a stay of liquidation, a liquidator has no authority over the company's property and in no circumstance has rights to do anything with the company's documents. The Court concluded that, at very least, the liquidator should have applied to the Court for directions
- Once the liquidator comes into possession of material that is clearly private to individuals, a duty of confidentiality arises
- The awareness of the private nature of the material is relevant in assessing the liquidator's conduct. Mr Walker was not held liable for breach of confidence in relation to a distribution of a tape drive containing private information to the IRD because the High Court was convinced that Mr Walker could not know at the point of distribution about the private content
- The fact that someone stores private documents in a company laptop does not preclude an expectation of privacy
- Mr Walker transmitted to the Official Assignee a flash drive containing all the emails and voice recordings found on the laptop. The Court determined that the liquidator was justified on public interest grounds in disclosing some of the information (for example information that suggested that Mr Henderson was in breach of the conditions of his bankruptcy). However, that did not permit the liquidator to disclose the contents of the laptop carte blanche. Only the relevant material should have been provided.

The High Court dismissed claims related to conversion, misfeasance in public office, breach of statutory duty and contempt and declined to order Mr Walker to provide a schedule of material accessed, indicating to whom it has been distributed.

The decision is one which all insolvency practitioners should take note of and become familiar with, as it outlines important obligations owed by those practitioners to private individuals whose data they come into the possession of in the course of their assignments.

The decision can be found [here](#).

---

### Potential liquidation no excuse for not paying overdue court costs

The High Court in *Cullen Group Limited v Commissioner of Inland Revenue* [2019] NZHC 3110 has rejected Cullen Group's attempt to delay payment of half a million dollars in court costs to the Commissioner of Inland Revenue, with Palmer J dismissing the argument that Cullen Group would go into liquidation as a result.

Eric Watson's private investment company, Cullen Group Limited, lost a case in front of Palmer J in March which held that Cullen Group avoided \$51.5m of tax. Cullen Group owed Inland Revenue \$505,399.55 in court costs.

Inland Revenue issued a statutory demand for the amount of the costs award, which had remained unpaid for almost eight months. Cullen Group sought to stay the enforcement of costs and set aside the statutory demand and application that it be placed into liquidation.

Cullen Group argued that it had insufficient liquid assets to pay costs now, but was in the process of an asset sale which should yield roughly \$1m in proceeds in February. Palmer J did not accept this argument, noting that while the Cullen Group accounts showed negative equity, its subsidiary, Cullen Investments, had ample funds to pay the costs award. The award would only tip Cullen Group into insolvency if it chose to do so, and Cullen could not force a stay of payment of the judgment costs by threatening its own liquidation.

The decision can be found [here](#).

---

## Liquidation applications are not to be refused lightly

The Court of Appeal in *90 Nine Limited v Luxury Rentals NZ Limited* [2019] NZCA 424 allowed an appeal from a creditor in respect of an application to liquidate the respondent over a failure to pay a statutory demand.

Following assignment of the benefit of a debt, the appellant had issued a statutory demand for \$1,000 to the respondent. The respondent failed to pay the amounts owing. The appellant then applied to the High Court to liquidate the respondent. In the High Court the application was rejected on the basis that the costs of a liquidation would be disproportionate to the indebtedness for which the proceeding was issued.

The Court of Appeal disagreed with the High Court and held that the application should be accepted. The prescribed minimum value for a statutory demand under the Companies Act 1993 is \$1,000. The Court also considered that given the respondent had failed to pay the demanded amount, there was appropriate 'standing' for the appellant to apply to liquidate and the court should only exercise its discretion to refuse a liquidation application sparingly. The Court also wished to endorse the statutory demand process and considered that the process may be undermined if applications to liquidate could be easily refused. It was also satisfied there was no abuse of process.

The decision can be found [here](#).

---

## Court approves of using liquidation proceedings as a method of debt collection

The Insolvency and Company Court of England and Wales recently held in *Sell Your Car With Us Ltd v Anil Sareen* [2019] EWHC 2332 (Ch) that, when a debtor fails to comply with a statutory demand and has no arguable case to dispute a debt, a winding-up petition (initiation of liquidation proceedings) is appropriate, despite judges previously expressing distaste towards the use of a petition as a method of debt collection.

The case involved the defendant company, Sell Your Car With Us Ltd, inadvertently paying money owed to Mr Sareen into the bank account of a fraudulent third party who had intercepted Mr Sareen's emails. Via statutory demand, Mr Sareen then required the company to pay the sale proceeds into his correct bank account and, after they failed to do so, initiated a winding-up petition to recover the debt.

In response, the company sought to restrain the petition on grounds that there was not a debt owing due to Mr Sareen being responsible for the fraud. They further submitted that, if the debt did exist, the threat of a winding-up petition should not be used as a method of debt collection.

The court held that the company alone was responsible for the payment to the fraudster due to a failure to implement checks on the third party's purported identity. This meant that the debt was undisputed, and Mr Sareen, as an unpaid creditor, was fully entitled to initiate a winding-up petition.

The English courts "have historically looked dimly" on the use of liquidation proceedings in this way. The present case affirms a more modern and pragmatic approach: a failure to pay even a single small debt is evidence that the company is unable to its debts as they fall due, which is the basis of liquidation. New Zealand's process for initiating liquidation proceedings is similar the United Kingdom's, and New Zealand courts have moved to adopt the more pragmatic approach now signalled in the UK.

The full decision can be found [here](#).

---

## Marshalling the securities of priority creditors: Protecting secondary mortgagees

In a decision that will be welcomed by secondary mortgagees, the Victoria Court of Appeal in *Burness v Hill* [2019] VSCA 94

clarified the availability of marshalling in Australia. The Court enabled a second mortgagee, whose debt had not been paid from the sale of the mortgaged property, to access the proceeds of sale of other properties mortgaged by the same debtor to the same primary mortgagee. The Court found that this was only precluded if the primary mortgagee was legally bound to look first to the commonly mortgaged property to satisfy its debt.

Hill, held a secondary mortgage over a property belonging to his client, Love, to secure unpaid legal fees. The Commonwealth Bank (CBA) held a first ranking mortgage over that property and other properties owned by Love. The CBA sold the commonly mortgaged property. No proceeds were left from that sale to satisfy Hill's debt.

The Court found that Hill could access the proceeds of sale from the other mortgaged properties despite the fact CBA was neither arbitrary nor capricious in its decision to sell the commonly mortgaged property. For this to have been prevented, CBA would have had to be legally bound to look first to the commonly mortgaged property. CBA and Love had a non-binding agreement that CBA would sell the commonly mortgaged property first to satisfy its debts. This was not sufficient.

Although this is an Australian case, it is instructive as to how the Courts are likely to approach this issue in New Zealand as the two jurisdictions have a similar approach to marshalling.

The decision can be found [here](#).

---

## Court of Appeal clarifies guarantee requirements

*Regan v Brougham* [2019] NZCA 401 clarifies what is needed to establish a valid guarantee.

A Term Loan Agreement was entered into whereby Christine Regan and Mark Tuffin lent \$50,000 to B & R Enterprises Ltd. Rachael Dey and Bryce Brougham were named as Guarantors. Bryce Brougham was the only guarantor to sign the agreement. The Company was put into liquidation and a demand made against the Guarantor.

The guarantor argued that the guarantee was not enforceable based on the following:

- Shortly before the Agreement was signed, Dey said she would not be signing the guarantee, this was an oral variation of the agreement and therefore did not comply with s 27(2) of the Property Law Act 2007
- The Agreement contemplated two guarantors, and only one signed, rendering the guarantee unenforceable
- A separate deed of guarantee was contemplated as a condition precedent and this was never executed. Therefore, there was insufficient detail in the Agreement to constitute an enforceable guarantee.

The Court disagreed. It held that discussions prior to signing the Agreement are not relevant; under s 27(2) of the Property Law Act, the guarantee was signed and in writing, rendering it valid and enforceable. Although there was provision for more than one guarantor, each guarantor was jointly and severally liable. The fact that one did not sign the guarantee did not mean it was invalid and unenforceable. Finally, the Court held that the Appellants waived the condition precedent as they did not think it necessary to have a separate deed of guarantee.

The decision can be found [here](#).

---

## High Court finds former director personally liable to creditor pursuing a claim for unpaid work

The High Court in *DHC Assets Ltd v Arnerich* [2019] NZHC 1695 recently considered an application under s 301 of the Companies Act (the Act) seeking to recover \$1,088,156 against the former director of a liquidated company (Vaco). The plaintiff had a construction contract with Vaco and said it had not been paid for all the work it performed under that contract.

The plaintiff argued that Mr Arnerich had breached his director's duty under s 131 of the Act. The Court confirmed that while the s 131 duty is owed to the company, this may require directors to consider creditors especially if the company is of doubtful solvency. The Court held that when Mr Arnerich distributed all of Vaco's assets to a trust rendering the company insolvent, he was not acting bona fide and in good faith. As he was clearly aware the plaintiff was pursuing claims that it had not been paid in full, Mr Arnerich breached the duty in s 131.

The court also confirmed that, with reference to *Levin v Ikiua*, that the corporate trustee position of Vaco did not afford Mr Arnerich any protection from liability as a director of Vaco.

The Court considered this was an appropriate case for Mr Arnerich to compensate the plaintiff directly, when the plaintiff had pursued the case and the liquidator had elected not to do so. Nevertheless, it only awarded a portion of the claimed amount, being the amount found owing in prior adjudication proceedings commenced under the Construction Contracts Act. The final amount of Vaco's indebtedness to the plaintiff had to be determined through arbitration proceedings which had been initiated but

had been adjourned.

This case provides a useful caution to plaintiffs to ensure that the full extent of liability owing by directors has been determined in accordance with contractual dispute resolution clauses before bringing a claim pursuant to s301.

The decision can be found [here](#).

---

## **Madoff "feeder fund" insolvency: Court unwilling to restrict application of domestic insolvency legislation in cross-border liquidation**

The Privy Council has rejected an attempt to block a cross-border liquidation on procedural grounds in *UBS AG New York v Fairfield Sentry* [2019] UKPC 20.

Fairfield Sentry Ltd (Sentry) was one of a number of British Virgin Islands 'feeder' funds for Bernard L. Madoff Investment Securities, the central entity in Bernie Madoff's Ponzi scheme. Sentry was put into liquidation following the revelation of Madoff's fraudulent behaviour, and the liquidators set about pursuing investors in the scheme who had profited from their shareholding. UBS was one such investor, having redeemed shares between 2004 and 2008.

This proceeding was an appeal from the Eastern Caribbean Supreme Court, which had rejected an application by UBS for an anti-suit injunction restraining Sentry's liquidators from pursuing proceedings in the United States under section 249 of the BVI Insolvency Act 2003. Section 249 allows the High Court of the BVI (High Court) to set aside voidable transactions.

UBS's main argument was the section 249 conferred a power on the High Court alone, as that was the court charged with supervising the liquidation. This argument had previously failed in proceedings in the United States.

The liquidators argued that the application of BVI law was a matter for the United States courts to determine. They also argued that the re-litigation of the issue in the BVI courts was an abuse of process, and that UBS had not provided any basis to block the injunction.

The Privy Council dismissed the appeal.

The decision can be found [here](#).

---

## **Australian insolvency practices to undergo ombudsman inquiry**

On 10 October 2019 the Australian Small Business and Family Enterprise Ombudsman, Kate Carnell, announced an upcoming inquiry into insolvency practices. The inquiry was announced in light of rising concerns as to the efficacy of the voluntary administration process for SMEs and family-owned businesses, and concerns with the conduct of insolvency practitioners more generally.

In the announcement Ms Carnell acknowledged that the voluntary administration scheme had only been successful for a very small number of SMEs, and that the insolvency process often had a devastating effect on the small business owner (including family owned business).

The inquiry will consider four key aspects of the insolvency sector:

- The existing insolvency system, through the experience of small businesses
- The level of transparency of governance, processes and costs of practitioners including legal advisers, valuers, investigating accountants, administrators, receivers and liquidators
- How the insolvency of a small or family business may lead to bankruptcy for the owners
- How the framework impacts the practices and fees of insolvency practitioners.

The New Zealand voluntary administration regime is largely based on the Australian one, so any recommendations will be of interest for New Zealand.

A summary of the inquiry can be found [here](#).

---

## **Business rates avoidance schemes: Dismissal of public-interest winding-up petitions**

In *Secretary of State for Business, Energy and Industrial Strategy v PAG Asset Preservation Ltd* [2019] EWHC 2890 the Secretary presented petitions under s 124A of the Insolvency Act 1986 to wind up two companies on public interest grounds. These companies were PAG Asset Preservation Limited and MB Vacant Property Solutions Limited (the Companies).

The Companies operated schemes for the avoidance or mitigation of national non-domestic business rates. It was alleged that the

schemes abused and/or subverted the insolvency legislation, so the Companies ought to be wound up.

The Companies allowed landlords to avoid paying business rates by leasing property to a special purpose vehicle (SPV) incorporated by the Companies that was then placed into members' voluntary liquidation.

The Court refused the application to wind up the Companies and held that the combined provisions of sections 91(1) and 107 of the Act justified the conclusion that the purpose of a voluntary liquidation, whether by members or creditors, was to collect, realise where necessary, and distribute assets. So long as it could be demonstrated by reference to objective evidence that the purpose of the voluntary liquidation was the collection, realisation and distribution of genuine assets, the motives of those involved were irrelevant.

The Court held that the incorporation or acquisition of the SPVs, the entry into the leases and the placing of an SPV into voluntary liquidation was not a sham transaction. It considered that there must be more to show that the operators were not acting with commercial probity or were acting contrary to the public interest.

The decision can be found [here](#).

---

## Media: One more big case to go for Madoff bankruptcy trustee and success story of Lehman Bros Europe administration

Bloomberg reported last month that the Madoff bankruptcy has one more big case to go, chasing USD3.2b held by foreign banks (see our related story above). Mr Picard, the bankruptcy trustee, has reportedly recovered over USD14b of the USD17.5b in losses arising from Madoff's Ponzi scheme.

Bloomberg also reports that the trustee and his various lawyers and consultants have earned over USD1.8b in fees over the 11 years of the bankruptcy. This puts it on a par with the administration of Lehman Brothers International (Europe), the combined administrators' and legal fees for which was over £1.5b at September 2019. That is another significant success story, with all investors repaid their principal and interest. Source material [here](#) and [here](#).

---

### Auckland

188 Quay Street  
Auckland 1010

PO Box 1433  
Auckland 1140  
New Zealand

P: +64 9 358 2555  
F: +64 9 358 2055

### Wellington

Aon Centre  
1 Willis Street  
Wellington 6011

PO Box 2694  
Wellington 6140  
New Zealand

P: +64 4 499 4242  
F: +64 4 499 4141

### Christchurch

83 Victoria Street  
Christchurch 8013

PO Box 322  
Christchurch 8140  
New Zealand

P: +64 3 379 1747  
F: +64 3 379 5659