**IN THE HIGH COURT OF NEW ZEALAND**
**AUCKLAND REGISTRY**

**CIV-2014-404-2511**
**[2016] NZHC 1691**

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| UNDER | Part 19 of the High Court Rules and section 34 of the Receivers Act 1993 |
| IN THE MATTER | of H.B. Garments Limited (in Liquidation and in receivership) and HAD Garments Limited (in liquidation and in receivership) |
| BETWEEN | ANDREW JOHN MCKAY<br>Applicant |
| AND | CLIVE ASHLEY JOHNSON<br>First Respondent (Discontinued) |
| | GEOFF MARTIN SMITH<br>Second Respondent |

Hearing: 10 March and 9 June 2016
Further submissions received 16 June and 5 July 2016

Appearances: R B Stewart QC and J Caird for the Applicant
First Respondent discontinued
Second Respondent in person (debarred from defence)

Judgment: 25 July 2016

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## JUDGMENT OF MUIR J

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*This judgment was delivered by me on Monday 25 July 2016 at 4.00 pm pursuant to Rule 11.5 of the High Court Rules.*

*Registrar/Deputy Registrar*

*Date:…………………………….*

Counsel/Solicitors:
R B Stewart QC, Barrister, Auckland
J C Caird, Simpson Grierson, Auckland

Copy to: Second Respondent

## Introduction

[1] In these proceedings Mr McKay, who was on 6 August 2014 appointed receiver of HAD Garments Ltd (In Liquidation and Receivership) (HAD) and H.B. Garments Ltd (In Liquidation and Receivership) (HB) (together, the Companies) by Westpac NZ Ltd (Westpac), seeks orders that Mr Smith, the Companies' liquidator, pay him;

(a) The sum of $540,666.82; and

(b) Interest on that sum at the prescribed rate under the Judicature Act from the date of his receivership.

[2] The claim has a lengthy procedural history which I will set out in some detail because it provides necessary context to the "unless" orders made by me on 10 March 2016, requiring payment by Mr Smith of the sum of $2,500 costs to Mr McKay by 28 April 2016, in default of which he was to be debarred from further defence of Mr McKay's claims. This was the third occasion on which unless orders had been made against him during the interlocutory stages of the proceedings. In the event, the costs order was not paid by 28 April 2016 (or subsequently).

[3] At the resumed hearing on 9 June 2016 Mr Smith again appeared in person. I indicated to him that he was now debarred from further defence of the claim which would proceed on a basis analogous to that of formal proof, albeit that I would consider the affidavit evidence filed by him and already before the Court. Mr Smith was invited to remain in Court while Mr McKay presented his case, however he chose to leave, requesting the Court record show that he was "a living natural man subject to common law". In a bench note dated 8 June 2016 I set out the relevant exchange in greater detail.

[4] The issue which I am required to decide is whether Mr McKay has, on the balance of probabilities, made out his claims that Mr Smith has received monies belonging to the Companies and secured to Westpac and which he has, without

lawful justification, failed to account to Westpac for. If so, I am required to determine the quantum of the payment Mr Smith must make to Mr McKay as receiver.

**Background**

*The security dispute*

[5] At the time of Mr McKay's appointment as receiver of the companies:

(a) The first respondent (Mr Johnson) had been appointed by GFH Properties Ltd (GFH) (to which securities held by Bank of New Zealand had been assigned) as receiver of HB.

(b) Mr Smith had been appointed by the company shareholders as liquidator of the Companies. That occurred on 5 November 2013.

[6] The parties were in dispute as to who had priority to the assets of the Companies with Mr Smith and Mr Johnson disputing the validity of Mr McKay's appointment.

[7] Westpac had first become aware of Mr Smith's position as liquidator on or about 11 March 2014 when it received his first liquidator's reports for the Companies. Those reports had incorrectly recorded Westpac as an unsecured creditor.

[8] On 13 March 2004 Westpac wrote to Mr Smith advising him that:

(a) It was a secured creditor of the Companies.

(b) It required the liquidator's first reports to be immediately amended to record its status as such.

(c) (Importantly) in dealing with the Companies' assets in the course of the liquidations Mr Smith was required to protect Westpac's security interests at all times and that its approval was required before any of

the Companies' assets were disposed of and that full sale proceeds were to be accounted to Westpac.

[9] Westpac's position was based on a general security agreement (GSA) (dated around 1995 but unable to be located) over HB, a second GSA over HB dated 22 June 2010 and a GSA over HAD dated 26 May 2003.

[10] Correspondence followed between the parties in which Mr Smith declined to acknowledge Westpac's status as a secured creditor.

[11] Accordingly, Mr McKay brought the present proceedings seeking declarations from the Court as to:

(a) Whether his appointment was valid;

(b) Whether he was entitled to possession of the Companies' assets; and

(c) If so, whether Mr Smith was liable to pay compensation to Mr McKay/Westpac for dealing with the Companies' assets during the period for which he was appointed as a liquidator.

[12] Mr Smith did not oppose Mr McKay's application in so far as it sought confirmation of the validity of Mr McKay's appointment and his entitlement to possession of the Companies' assets, recording that position in documents filed with the Court. Accordingly, the matter proceeded to a formal proof hearing on 23 February 2015 before Fogarty J. He delivered an oral judgment holding that:[1]

(a) Westpac's security over the Companies by way of GSAs was valid and enforceable;

(b) In respect of the assets of HB, Westpac's security interest had priority over GFH's security interest except in respect of seven trucks in

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1 *McKay v Johnson* [2015] NZHC 242.

relation to which Westpac conceded its security was second ranking to that of GFH;

(c) Mr McKay was validly appointed as receiver and manager of the Companies; and

(d) Mr McKay was entitled to take possession and control of the assets of the Companies (with the exception of the seven specified trucks).

[13] The Court reserved for later determination the remaining issues, namely whether Messrs Smith and Johnson were required to pay Mr McKay compensation for any loss suffered while the Companies' assets were in their possession and control and what, if any, costs were payable. His Honour made timetable orders for disposition of those issues. Relevantly, Mr Smith was to file an affidavit by 9 March 2015 setting out:

(a) Details of any of the Companies' assets that he had dealt with since his appointment as liquidator, including the current status of those assets;

(b) Details of any of the Companies' assets previously in his possession or control that had been realised, disbursed or destroyed; and

(c) Details of all remuneration and expenses he had incurred during liquidation and the extent to which any of the Companies' assets had been used to pay such remuneration and expenses.

[14] Paragraph [6] of Fogarty J's judgment is usefully set out in full. It was in terms:[2]

> [6] Accordingly, for these reasons, I grant the orders sought in the notice of originating application dated 23 September 2014 in paras (a), (b), (c) and (d). As to (e), there will be an enquiry as between the applicants and the first and second respondents as to whether there is an obligation by them and/or BNZ to pay to the applicant receivers and/or Westpac funds recovered by them on the assumption that they had priority.

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[2] *McKay v Johnson* above n 1.

[15] I set this paragraph out because it answers the often repeated allegation in Mr Smith's subsequent affidavits that the judgment of Fogarty J related only to Mr McKay's entitlement to company assets which existed on or after Mr McKay's appointment. To the contrary, the judgment of Fogarty J expressly recognised that Mr McKay's claims extended to the assets of the company (including monies recovered from its debtors), which existed prior to his appointment as receiver during the period that Messrs Johnson and Smith acted respectively as receiver and liquidator of relevant entities.

[16] Mr McKay has subsequently settled with Mr Johnson and has filed a notice of discontinuance in that respect. I do not therefore refer further to Mr Johnson's involvement, except as necessary.

[17] Although Mr Smith filed his affidavit on 9 March 2015 as directed by Fogarty J, it was regarded as deficient by Mr McKay in not providing sufficient detail of the Companies' assets currently or previously in the control of Mr Smith or details of expenses. Requests were made for Mr Smith to provide further information. He did not do so.

[18] Furthermore Mr Smith failed to comply with his statutory reporting obligation to file reports in respect of both companies at six monthly intervals. That statutory source of information was therefore similarly unavailable to Mr McKay.

[19] The matter reverted to Fogarty J on 19 August 2015 when he made timetable directions for the filing of further affidavit evidence and written submissions and directed a one day fixture, subsequently allocated for 9 November 2015. Mr McKay complied with the relevant timetable orders. However, Mr Smith neither filed reply evidence in accordance with Fogarty J's directions nor written submissions. The matter was accordingly placed in a Duty Judge List on 5 November 2015 to consider Mr Smith's noncompliance with timetable directions. Wylie J ordered Mr Smith to file and serve any affidavits on or before 12 pm on 6 November 2015 on the basis that, if he defaulted, his defence to the proceeding was set aside. This was therefore the first occasion on which Mr Smith was subject to "unless" orders.

[20] Mr Smith's affidavit was filed and served on 6 November (apparently shortly after 12.00 pm although no point was taken). In it he made the surprising claim (never previously advanced) that on 21 December 2013 he had sent to Mr Chinniah at Westpac a notice pursuant to s 305 of the Companies Act 1993 requiring Westpac's election, in default of which its security would be deemed abandoned. He claimed that Westpac had abandoned its security accordingly. He also claimed that Mr McKay and Ms Stone (a senior employee of BDO Auckland assisting Mr McKay with the receivership) were advised of the s 305 notice at a meeting on 14 August 2014. Annexed to the affidavit was a letter from Mr Smith addressed to Ms Stone, purportedly dated 14 August 2014, recording discussions at that meeting, including the reference to the s 305 notice.

[21] In the result, Mr Smith claimed:

(a) Westpac's security was invalid.

(b) Mr McKay's appointment was invalid.

(c) Mr McKay and his counsel did not put all relevant information before Fogarty J at the hearing on 23 February 2015.

(d) Mr McKay's proceeding was "illegal".

(e) The judgment of Fogarty J dated 23 February was "faulty".

[22] Despite this attack on the judgment of Fogarty J, neither any appeal from it nor application to recall it has been lodged or made.

[23] As a consequence of matters raised by Mr Smith in his 6 November 2015 affidavit Mr McKay reluctantly sought an adjournment of the hearing scheduled for 9 November 2015. Mr Smith also sought an adjournment on the basis he needed more time to complete his affidavit evidence.

[24] Toogood J ordered that the hearing be adjourned on consent terms, including that Mr Smith:

> … consents to the applicant obtaining copies of all bank accounts with Bank of New Zealand in the name of the Companies or Geoff Smith Liquidations Limited or similar account names and they correspond directly with Bank of New Zealand to obtain the same.

[25] This order allowed Mr McKay to access relevant information from the "liquidation accounts" opened by Mr Smith and into which the Companies' funds had been transferred by Mr Smith during the course of liquidation of the Companies. That was information not previously available to Mr McKay.

[26] Toogood J also made "unless" orders requiring Mr Smith, by 17 November 2015, to deliver to the offices of Simpson Grierson various computers and requiring any further affidavits by him to be filed by 2 December 2015. Paragraph [3(i)] of his Honour's orders stated that Mr Smith was to be "automatically debarred from opposing the application" if such timetable orders were not complied with. This was therefore the second occasion on which Mr Smith had been subject to "unless" orders.

[27] On 1 November 2015 Mr Smith sought an extension of the time for the filing of affidavit evidence. This was declined by Edwards J although he was allowed to file an unsworn copy of this proposed affidavit by 2 December with a sworn copy to follow. Mr Smith's sworn affidavit was filed on 3 December. It repeated the allegation in his November 2015 affidavit that a s 305 notice had been delivered to Westpac on 21 December 2013. He annexed copies of the purported notice. He also annexed photographs marked "G" as purported proof of service of the notice on Westpac.

[28] Mr McKay formed the view that both the s 305 notice and letter to Ms Stone dated 14 August 2014 were created significantly later than the dates deposed to by Mr Smith. He did so on the basis:

(a) The photographs which Mr Smith annexed to the December affidavit as proof of delivery of the s 305 notice on 21 December 2013 were taken some time after 7 October 2015 as they depicted envelopes with "New Zealand's longest reigning monarch" commemorative stamp which was only issued by New Zealand post on 7 October 2015.

(b) Mr Smith had provided no proof of delivery of the purported letter to Ms Stone.

(c) Neither Mr McKay, Mr Chinniah nor Ms Stone had seen the purported s 305 notice prior to Mr Smith's November 2015 affidavit nor the purported letter of 14 August 2014.

(d) There was no reference in either Westpac's or its receivers' files to the notice or letter.

(e) Messrs McKay, Chinniah and Ms Stone were all fully aware of the significance of such a notice.

(f) The purported s 305 notice was dated 21 December 2013 and addressed to Mr Chinniah. However, Mr Chinniah's first contact with Mr Smith was on 13 March 2014 when he wrote pointing out that Westpac was a secured creditor, contrary to the reference in Mr Smith's report.

(g) If the s 305 notice had been sent in December 2013 then inevitably Mr Smith would have raised that as a ground for opposing Mr McKay's application for orders confirming Westpac's security and the validity of his appointment as a receiver of the Companies. Such notice would have been determinative because, in the absence of election, Westpac would prima facie have been held to have surrendered its securities.

(h) Mr Smith had a history of dishonesty, including convictions for tax evasion, theft, fraud and falsifying documents.

[29] Accordingly, on 10 December 2015 Mr McKay applied, without notice, for orders permitting inspection of the purported letter and notice by a computer forensic expert Mr B P Whale. That application was supported by evidence from Mr McKay, Mr Chinniah and Ms Stone in the terms referred to above. On 10 December 2015 Brewer J granted orders as moved and on 14 December 2015 inspection occurred

under the supervision of an independent barrister. Mr Whale has subsequently filed an affidavit confirming that both the s 305 notice and the letter were created on 26 October 2015, that is, shortly before the claims first made in Mr Smith's November 2015 affidavit.

[30] In response to this evidence Mr Smith filed an affidavit from Mr P R Shortt. Mr Shortt states that he agrees with Mr Whale "except with his final synopsis and analytical conclusion that in my opinion causes professional confusion". He states that:

> The two RTF files therefore containing data were created on this specific date and time by G M Smith. However, the source of the data stored within these two RTF files is not recorded within the file system and the document metadata and therefore their original source, date, time and original author cannot be determined.

[31] He invited the Court therefore to conclude that although the relevant documents were created on the dates specified by the applicant that could have been on the basis of documents earlier imported to Mr Smith's computer.

[32] I do not accept the evidence of Mr Shortt. Although he claims to be a "suitably qualified forensic accountant and computer and systems analyst of 30 years experience" he sets out no professional qualifications or relevant work history. Moreover, although required to be produced for cross-examination of his affidavit at the resumed hearing he did not so appear. I am satisfied therefore, on the balance of probabilities, that the purported s 305 notice and letter to Ms Stone were created on dates significantly later than those deposed to by Mr Smith.

[33] Mr Smith challenged the legality of the inspection order. On 17 December 2015 Duffy J made timetable orders requiring, among other things, that Mr Smith file a formal application by 21 December 2015. He did not do so. In the interim Mr McKay's application for determination of his compensation claims was set down for hearing on 10 March 2016. On 5 February 2016 Mr McKay filed an affidavit incorporating his review of the bank statements made available to him by Mr Smith and setting out the quantum of the compensation he sought. That affidavit remains the basis of his claim. On 25 February he filed his synopsis of submissions.

[34] Because of Mr McKay's unavailability on 10 March he was cross-examined by Mr Smith before the Registrar on 1 March 2016. That cross-examination was on the various affidavits filed by Mr McKay up to that point. I have reviewed the transcript.

[35] On 26 February 2016 Mr Smith belatedly filed his application to rescind the order for inspection. Two days earlier he had served orders of subpoena on Mr McKay's solicitors and counsel and Mr Allan, a case manager at the High Court in Auckland.

[36] The matter came before Whata J in the Duty Judge List of 2 March. He:

(a) granted applications by Mr McKay setting aside the orders for subpoena; and

(b) made timetable orders for the filing and serving of evidence and submissions in relation to the rescission application so as to facilitate disposal of it on 10 March 2016, together with Mr McKay's substantive claim.

[37] Mr Smith filed affidavits in support of the rescission application and on 8 March Mr McKay filed his notice of opposition and affidavits. Then, on the eve of the hearing, Mr Smith filed an affidavit in relation to the compensation claim responding in part to Mr McKay's affidavit of 5 February 2016.

[38] The matter came before me on 10 March. I declined the rescission application with reasons to follow.[3] I then heard and granted an application by Mr Smith for leave to file his affidavit of 9 March out of time.[4] In my oral decision I recorded (noting the agreement of Mr Stewart QC for Mr McKay in this respect) that the efficient administration of justice should not trump the overall interests of justice and that for Mr Smith's defences to be properly ventilated there needed to be an

[3] The reasons decision is *McKay v Johnson & Smith* [2016] NZHC 466 [*Reasons*], given on 17 March 2016.

[4] *McKay v Johnson & Smith* [2016] NZHC 410 [*Application for leave to file affidavit out of time*].

evidential foundation for which Mr Smith was relying, inter alia, on his affidavit of 9 March 2016.

[39] I recorded Mr Stewart's position that if the affidavit was admitted, then inevitably the matter would need to be adjourned to give Mr McKay a proper opportunity to respond.

[40] I made timetable orders requiring, among other things, that any further affidavits by Mr Smith in opposition be filed by 4.30 pm on 31 March 2016. I then addressed the issue of costs. In the context of what I described as an "indulgence" I stated:[5]

> [18] Mr Stewart applies for costs in the amount of $3,000. His application is, in my view, unanswerable. This fixture has been effectively "hijacked" by last minute filing only permitted because of my concern about the overall interests of justice on what is a substantial claim against an unrepresented litigant. It is inevitable that the applicant will sustain significant additional legal costs arising out of the adjournment. Delay and cost go hand in hand.

[41] In the event, I awarded costs in the amount of $2,500. I then stated:

> [19] … Because of the history of these proceedings and my concerns that these may not be paid absent appropriate incentives, an "unless" order is in my view appropriate.
>
> [20] Accordingly, unless the said sum of $2,500 is paid to the applicant's solicitors, Simpson Grierson, Auckland, by 28 April 2016 the second respondent is to be debarred from further defence of the applicant's claims.
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> [21] Mr Caird is, within 24 hours, to supply Mr Smith with relevant banking details for remittance of that sum.

[42] I have received confirmation that the relevant banking details were supplied in terms of [21].

[43] Subsequently, and in response to a memorandum from Mr Smith, I allowed an extension of time for his affidavits to 8 April 2016. Additional affidavits were accordingly filed by him on 31 March and 8 April 2016. However, the order for costs made by me was not complied with either by 28 April or subsequently.

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5 *McKay v Johnson & Smith* [*Application for leave to file affidavit out of time*], above n 4.

Accordingly, Mr Smith became debarred from further defence of Mr McKay's claims on 29 April 2016.

## Relevant legal principles

*Secured creditors and liquidations*

[44] Secured creditors are for the most part regarded as falling outside the liquidation process as prescribed under Part 16 of the Companies Act 1993 (the Act). As the Court of Appeal stated in *Dunphy v Sleepyhead Manufacturing Co Ltd*:[6]

> The scheme of Part 16 of the Companies Act is to exclude from the ambit of the liquidation property which is subject to a charge. The Act contemplates that secured creditors will operate independently of the liquidation, unless they decide to surrender their security in terms of s 305(1)(c). The definition of "creditor" in s 240(1) makes it clear that secured creditors are excluded except for very limited purposes, … Section 248(2) makes it clear that the liquidation does not limit the secured creditors' rights of enforcement, and s 253 provides that the liquidator's principal duty is to take possession of the assets and distribute them or their proceeds to "creditors" (which, for this purpose, excludes secured creditors)….

[45] A liquidator who does not account to a secured creditor for a secured asset is liable to the secured creditor for conversion.[7] Where the failure to account is in respect of money I accept Mr Stewart's submission that an action lies in money had and received. In his book *Civil Remedies in New Zealand*[8] Sir Peter Blanchard notes:

> The claim for money had and received is available to reverse the defendant's unjust enrichment where the subject matter of the enrichment was money….
>
> … Money had and received appears to serve much the same role in respect of money as conversion serves in respect of tangible chattels.

[46] A claim for money had and received does not depend on any proof of wrongdoing or impropriety on behalf of the recipient, or on ongoing retention of the money or its value.[9] The cause of action is complete when the money is received.

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[6] *Dunphy v Sleepyhead Manufacturing Co Ltd* [2007] NZCA 241, [2007] 3 NZLR 602 at [43].

[7] *Dunphy v Sleepyhead Manufacturing Co Ltd,* above n 6 at [13] and [49].

[8] Peter Blanchard (ed) *Civil Remedies in New Zealand* (2nd ed, Brookers, Wellington 2001) at 391.

[9] *Nimmo v Westpac Banking Corporation* [1993] 3 NZLR 218 (HC) at 238; *Torbay Holdings Ltd v Napier* [2015] NZHC 2477 at [164].

[47] In *Agip (Africa) Ltd v Jackson*, Lord Millett said:[10]

> … The common law claim for money had and received is a personal and not a proprietary claim and the cause of the action is complete when the money is received. With only limited exceptions, it is no defence that the defendant has parted with the money. The claim does not depend on any impropriety or want of probity on the part of the defendants.

[48] Although impropriety need not be established, nevertheless there must be some element of *unjustness* in the defendant retaining the monies received.[11] This will be satisfied when the defendant has no right to it.[12]

[49] As Lord Millet alluded to, there are limited exceptions to a claim for monies had and received; principally the change of position defence available at both equity and law.[13] As Lord Goff of Chieveley held in *Lipkin Gorman (a firm) v Karpnale Ltd*:[14]

> … where an innocent defendant's position is so changed that he will suffer an injustice if called upon to repay or to repay in full, the injustice of requiring him so to repay outweighs the injustice of denying the plaintiff restitution.

[50] His Lordship then stated:[15]

> It is, of course, plain that the defence is not open to one who has changed his position in bad faith, as where the defendant has paid away the money with knowledge of the facts entitling the plaintiff to restitution; and it is commonly accepted that the defence should not be open to a wrongdoer.
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> …
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> I wish to stress however that the mere fact that the defendant has spent the money, in whole or in part, does not of itself render it inequitable that he should be called upon to repay, because the expenditure might in any event have been incurred by him in the ordinary course of things.

[51] The defence of change of position is therefore:

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10 *Agip (Africa) Ltd v Jackson* [1990] Ch 265, [1989] 3 WLR 1367 (HL) at 1380.

11 Lord Goff and Gareth Jones *Goff & Jones The Law of Restitution* (7th edition, Sweet & Maxwell, London, 2007) at [1-013].

12 *Torbay Holdings Ltd v Napier,* above n 9 at [166] and [167].

13 Judicature Act 1908, s 94B; *National Bank of New Zealand v Waitaki International Processing (NI) Ltd* [1999] 2 NZLR 211 (CA) at 228.

14 *Lipkin Gorman (a firm) v Karpnale Ltd* [1991] 2 AC 548 (HL) at 479, cited with approval by Thomas J in *National Bank of New Zealand v Waitaki International Processing (NI) Ltd* [1999] 2 NZLR 211 (CA) at 228.

15 At 580.

(a) contingent on the defendant having acted in good faith;[16]

(b) not available where the defendant changed his or her position with knowledge of the facts entitling the plaintiff to restitution;[17] and

(c) of limited application.[18]

*The liquidator's role and responsibilities.*

[52] A liquidator has extensive powers and duties under the Act to carry out the liquidation of a company in a reasonable and efficient manner. As stated in *Heath & Whale*:[19]

> The liquidator has a unique legal status which it is difficult to describe with precision. It may be best described as principally an agent for the company who occupies a position that is fiduciary in some respects and who is bound by the statutory duties imposed by the Act.

[53] The learned authors continue:[20]

> The liquidator's relationship to the company is that of an agent. This is not a normal agency position because the liquidator controls the principal (the company) and has statutory duties under the Companies Act which are focused on protecting the interests of creditors. It is an agency subject to external rules and ethical obligations…
>
> The liquidator's position, while sometimes referred to as a "trustee" is better described as that of a statutory agent whose responsibilities are to perform obligations under the Act and to distribute property divisible among creditors in accordance with the statutory priorities. The liquidator does not hold assets in trust for unsecured creditors but has a fiduciary duty, arising out of the nature of the agency, to apply property in terms of the statutory requirements and recognised legal and equitable rights of third parties.

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16 *Lipkin Gorman (a firm) v Karpnale Ltd* [1991] 2 AC 548 (HL) at 580. This is still the case, regardless of whether the Privy Council's recent decision of *Dextra Bank & Trust Co Ltd v Bank of Jamaica* [2002] 1 All ER (Comm) 193 (PC) is followed in this jurisdiction. Lords Bingham and Goff rejected a "relative fault" concept into the defence of change of position, at [45]. Their Lordships nonetheless proceeded on the basis that the defendant must have changed his position in good faith, at [42].

17 *Lipkin Gorman (a firm) v Karpnale Ltd*, above n 16 at 580.

18 *Agip (Africa) Ltd v Jackson,* above n 10 at 1380; *Lipkin Gorman (a firm) v Karpnale Ltd*, above n 16 at 580.

19 Paul Heath and Michael Whale (eds) *Heath & Whale on Insolvency* (LexisNexis, Wellington, 2008) at [22.01].

20 At [22.3].

[54] A liquidator must keep accounts and records of liquidation.[21] Furthermore he or she must report at six monthly intervals. Whether appointed by the Court or by shareholders or directors of the company (pursuant to s 241(2)(a) or (b) of the Act) liquidators are to be treated as if they were officers of the Court.[22]

*The liquidator's remuneration and expenses*

[55] Although a liquidator has a right to charge reasonable remuneration and claim expenses payable from the assets of the company in liquidation, his or her claim to the assets of the company cannot take priority over the secured creditors' interest in them.[23] In *Covacich v Riordan*[24] the High Court noted that while a liquidator's role might extend beyond that of merely realising assets for the benefit of unsecured creditors and a liquidator may at times need to investigate the status of a secured creditor, he or she did so at their own peril. Fisher J stated:[25]

> The point was made by Johnston J *In re New Zealand Times Co Ltd (in Liquidation)* [1941] NZLR 677 at page 685 initially quoting James LJ *In re Regents Canal Iron Works Co*, *ex parte Grissell* (1875) 3 CHD 411-426;
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> "Those who render services to an insolvent company or insolvent person frequently find that they have to go without payment, and the liquidators should not have incurred disbursements for which they had no means of being reimbursed".
>
> And he points out that a liquidator should look into the matter before he incurs expenses and makes himself liable, and, I may add, should see where his remuneration is to come from, before he undertakes the duty which is, after all, entirely voluntary.

[56] An exception to that principle arises in respect of the so-called "salvage principle" which applies where a liquidator performs work to preserve or realise an asset secured to a creditor. In that circumstance the liquidator will obtain priority over the secured creditor in respect of the liquidator's costs and expenses incurred in the preservation, care or realisation of the secured asset. The rationale is discussed

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21 Companies Act 1993, s 253.
22 *ANZ National Bank Ltd v Sheahan* [2012] NZHC 3037, [2013] 1 NZLR 674 at [122]
23 *Buchler v Torbitt* [2004] 2 AC 298 (HL) at 306.
24 *Covacich v Riordan* [1994] 2 NZLR 502 (HC).
25 At 510 – 511.

in the recent High Court of Australia decision of *Stewart v Atco Controls Pty Ltd (in Liquidation)* where it was said:[26]

> A secured creditor may not have the benefit of a fund created by a liquidator's efforts in winding up without the liquidator's costs and expenses including remuneration of creating that fund first being met. To that end, equity will create a charge over the fund and priority to that as a secured creditor.

[57] Underpinning the principle is the notion that a "secured creditor cannot lay claim to the benefit of realised assets without the costs of the realisation being met".[27] As such, the work undertaken by the liquidator must result in an indisputable benefit to the secured creditor.[28]

[58] As the High Court of Australia confirmed, the principle will apply in the following circumstances:[29]

(a) Where there is an insolvent company in liquidation.

(b) The liquidator has incurred expenses and rendered services in realisation of an asset.

(c) The resulting fund is insufficient to meet both the liquidator's costs and expenses of realisation and a debt due to the secured creditor; and

(d) The secured creditor claims the fund.

**Analysis**

*Mr McKay's right to possession of the Companies' assets*

[59] The judgment of Fogarty J held that Westpac's GSA's were valid and enforceable and that Mr McKay was entitled to take possession and control of the Companies' assets. As such he was entitled to possession and control of all funds of

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26 *Stewart v Atco Controls Pty Ltd (in Liquidation)* [2014] HCA 15, (2014) 252 CLR 307 at [22].
27 At [16].
28 Peter Blanchard and Michael Gedye (eds) *The Law of Private Receiverships of Companies in New Zealand* (LexisNexis, Wellington, 2008) at 143.
29 *Stewart v Atco Controls Pty Ltd (in Liquidation)*, above n 26 at [23].

the Companies as monies secured to Westpac. His Honour's judgment recognised the necessity of an inquiry into whether Mr Smith was required to pay Mr McKay and/or Westpac funds already recovered by him. To that end, orders were made requiring Mr Smith to provide details of all assets of the Companies which he had dealt with since his appointment as liquidator and the extent to which any of the Companies' assets had been used to pay for his remuneration or expenses.

[60] In his affidavits of 9 March, 31 March and 8 April 2016 Mr Smith effectively attacks that judgment. He says that Mr McKay was invalidly appointed for reasons including the fact that his appointment was by a person not listed as an authorised attorney of the bank. I would not have found that argument persuasive, even if available, as there is no doubt the appointment was made by an officer of the bank acting on authority. However, the basis of my rejection of the argument is more fundamental. There are extant orders of the Court recording that Mr McKay was "validly appointed as receiver and manager [of the Companies] on 6 August 2014".[30] Mr Smith's challenge represents a collateral attack on the Court's orders. It must be rejected on that ground alone.

[61] I place in the same category the attack on Mr McKay's appointment by virtue of Westpac's alleged abandonment of its security following purported receipt of a notice under s 305 of the Act. Again, that involves a collateral attack. In addition, I am satisfied, on the balance of probabilities, that no s 305 notice was served on Westpac on 21 December 2013 as alleged by Mr Smith and that the purported notice was fabricated. I reach that conclusion having regard not only to the report of the applicant's forensic expert but all of the evidence adduced in support of Mr McKay's application for inspection orders. The fact that the notice was addressed to Mr Chinniah when Mr Chinniah's first contact with Mr Smith was not until approximately four months later and the fact that the photograph of alleged service depicts an envelope with a stamp not published until 22 months after the event, seem to me to be particularly persuasive. Moreover, if Mr Smith had sent any such notice, it is inevitable that the matter would have been raised in opposition to the orders sought before Fogarty J.

[30] Order dated 16 February 2015 para (c).

*Monies received by the liquidator*

[62] The Companies had three existing accounts with BNZ prior to Mr Smith's appointment (the pre-liquidation accounts). These were respectively an 00 account in the name of HB, an 00 account in the name of HAD and an 02 account in the name of HAD.

[63] The Companies' business involved the selling of goods out of trucks in (typically) low income neighbourhoods on credit terms requiring small payments over many months. This resulted in a large number of automatic payments and direct debit/credits received into the pre-liquidation accounts. Mr McKay deposes that between 5 November 2013 (the date of Mr Smith's appointment as liquidator) and 6 August 2014 (the date of Mr McKay's appointment as receiver) there were 25,819 transactions recorded in the pre-liquidation accounts. The net value of receipts in that approximately 39 week period was $837,833.89 indicating an average of approximately $21,482 per week in receipts during Mr Smith's control of the pre-liquidation accounts.

[64] Subsequent to his appointment, Mr Smith opened two further bank accounts (the liquidation accounts) being an 00 account in the name of HB and an 00 account in the name of HAD. Mr McKay deposes that Mr Smith regularly "swept" or transferred the Companies' funds from the pre-liquidation accounts into the liquidation accounts. Significantly, customer payments to the Companies were only paid to the pre-liquidation accounts, including during the period in which Mr Smith was in control of the Companies.

[65] I accept Mr McKay's proposition that if new business had been generated by the liquidator subsequent to his appointment receipts would, in the ordinary course, have been made to the post-liquidation accounts established by him. I accept also Mr McKay's analysis of the bank statements which shows that for the 39 week period between Mr Smith and Mr McKay's appointments, average weekly receipts were $4,760 per week less than for the 39 week period immediately prior to Mr Smith's appointment.

[66] Mr McKay deposes and I accept that although Mr Smith has alleged on a number of occasions that he introduced new customers to the Companies while he traded the businesses he has not provided any details or evidence to support that allegation and has refused or failed to provide Mr McKay with details of the Companies' customer lists despite request.

[67] Mr McKay concludes and I accept that the total sums received by the Companies between 5 November 2013 and 6 August 2014 were $919,786.54. This comprised accounts receivable of $837,830.89 and other miscellaneous credits as deposed to in para 50 of Mr McKay's affidavit in reply dated 22 April 2016.

*Monies disbursed*

[68] I accept also Mr McKay's evidence that during the same period Mr Smith disbursed amounts of $852,988.54 from those accounts.

[69] Such disbursements are in two categories:

(a) Payments which are identifiable from the bank account statements in the sense that the statements contain sufficient particulars or details for Mr McKay to have ascertained the apparent purpose of those payments. These total $312,585.72 as detailed in Schedule 1 to this judgment.

(b) Payments totalling $540,402.82, the application of which is not identifiable from the bank account statements.

[70] The sum referred to in [69(a)] is $264 more and the sum referred to in [69(b)] $264 less than that sought by Mr McKay at the hearing on 8 June. The difference arises out of my subsequent inquiry (by Minute dated 13 June 2016) in which I sought advice from Mr McKay about which, if any, of the invoices annexed as Exhibit C to Mr Smith's affidavit dated 9 March 2015 (excluding Mr Smith's own fees) were identified as paid in the bank statements of the Companies.

[71] In response to that Minute, Mr McKay deposed that in Mr Smith's own affidavit he had stated that the invoices were unpaid except "some of Mr Smith's fees". However, Mr McKay said that, on further analysis, it was "probable" that an account from Guardian Storage Tauranga Ltd for $264 was reflected in a payment in the same amount from the HB 00 account on 22 July 2014. To that end, he accepted that the identifiable payments should be increased by $264 and the unidentifiable payments decreased by a corresponding amount.

[72] In his further response Mr McKay also repeated that, despite his multiple requests, he had never received from Mr Smith any accounts, cheque books, requisitions or other documents from which the character of any of the other unidentifiable payments could be established.

[73] In relation to the identifiable payments, Mr McKay takes the position that, although the funds used to make them were secured to Westpac and Westpac never consented to payment, nevertheless he elects not to seek recovery of those amounts. Significantly, this allowance includes $150,459 for wages, salaries and payroll processing which was conducted through a payroll company known as "KeyLink". I note this point because of Mr Smith's claim that Mr McKay has failed to account for wages and salaries.

[74] In respect of the unidentifiable payments, Mr McKay divides these into three categories:

(a) The sum of $133,315.95 in respect of cheque payments to unidentified recipients.[31]

(b) The sum of $348,285.99 in respect of unknown payments with no descriptions. Of that sum $300,241.02 is made up of 92 transactions taking place in the liquidation accounts (that is accounts solely under Mr Smith's control) which were either withdrawals through a teller

[31] This sum having likewise been reduced by $264 in respect of the Guardian Storage Tauranga Ltd account.

(for example the cashing of a cheque drawn on the accounts) or foreign exchange transactions.

(c) The sum of $58,800.88 in respect of payments with the description "creditors" made to unidentifiable recipients.

[75] In respect of the total sum of $540,402.82, Mr McKay claims:

(a) Mr Smith had sole control of the pre-liquidation and liquidation accounts at all material times.

(b) The money in the pre-liquidation and liquidation accounts was secured to Westpac.

(c) Westpac did not consent to Mr Smith making the unidentifiable payments.

(d) Mr Smith had no entitlement to the funds of the Companies used to make the unidentifiable payments and that any claim to remuneration and expenses from the assets of the company was subject to Westpac's prior ranking security interest.

(e) Mr Smith has been enriched to the extent of the amount received and disbursed and that such enrichment is unjust as against Westpac which has lost the benefit of those funds.

[76] Mr Smith's response in his several affidavits is in terms:

(a) "It was impossible to conclude any correct financial information from the figures on the bank statements";

(b) That Mr McKay had quoted the figure of $852,988.54 being funds transferred into the liquidator's trading account but had also quoted $837,833.89 being the total funds in the receiving accounts and that accordingly there was a discrepancy;

(c) That Mr McKay had double-counted monies received;

(d) That he had incorrectly included transactions by including those in the period that Mr Johnson was appointed as a receiver of HB;

(e) Mr McKay's stated 25,819 credits to the account were false;

(f) The average weekly income in respect of the Companies was overstated; and

(g) The stated receipts of $837,833.89 were false on the basis that, on Mr Smith's assessment, HB's income for the relevant period was $356,440.53 only and his "rough estimate" of the Companies' total receipts was $500,000.

[77] In reviewing Mr Smith's several affidavits I agree with Mr Stewart's submission that, in relation to matters material, Mr Smith's assertions are inadequately substantiated. I accept Mr McKay's reply evidence in terms:

(a) In respect of Mr Smith's figure of $356,440.53, this relates to one company (HB) and is not even based on all transactions which took place in the relevant period.

(b) Mr Johnson is not responsible for any of the unidentifiable payments. The only unidentifiable payment that was made in the period between Mr Johnson's appointment as receiver on 24 July 2014 and Mr McKay's appointment on 6 August 2014 was made from the liquidation account of HB which was an account opened by Mr Smith and under his control.

[78] In respect of alleged double-counting, I accept that Mr McKay's calculations are based only on payments made out of the pre-liquidation and the liquidation accounts to third parties. Accordingly, any transfers between the pre-liquidation and liquidation accounts have not been included as part of the unidentified payments and as such no double-counting has occurred.

[79] Nor do I accept the alleged "discrepancies". Mr McKay deposes in para [50] of his reply affidavit:

> With regard to the alleged discrepancy in the figures … as outlined in my 5 February 2016 affidavit, the net value of receipts in respect of the Companies' accounts receivable was $837,833.89. However, the Companies received a total of $919,786.54 in the period from 5 November 2013 to 6 August 2014 as a consequence of the accounts receivable, and other payments made to the Companies…

[80] The pre-liquidation accounts also had opening balances in credit at the date of Mr Smith's appointment. All the Companies' funds and not just the Companies' funds which are a consequence of the accounts receivable were secured to Westpac. Accordingly, there is no discrepancy in that the total amount of payments out of the pre-liquidation and liquidation accounts of $852,988.54 (i.e. the unidentifiable payments together with the identifiable payments) exceeds the total amount of the accounts receivable being $837,833.89.

[81] Mr Smith also makes a number of generalised criticisms in terms that Mr McKay has failed to account for wages, PAYE and IRD payments and had insufficient information about his trading expenses to reach conclusions about the amount of compensation properly payable by him.

[82] I accept Mr McKay's primary submission that even if Mr Smith could demonstrate that some of the unidentifiable payments were properly trading expenses of the Companies, his claim to the assets of the Companies for payment of its trading expenses ranks behind Westpac as secured creditor.

[83] It is not necessary for Westpac to show wrongdoing or impropriety in terms of its claim for money had and received, simply "injustice" in the assertion by Mr Smith of rights to that money. I consider such injustice made out. Mr Smith acted at his peril in choosing not to recognise Westpac's security over payments received to the Companies accounts. Without prior correspondence with the Bank, he applied monies subject to that security for payment of at least part of his fees and in the identifiable and unidentifiable ways Mr McKay records. From 13 March 2014 (being two days after Westpac first became aware of his appointment) he was on specific notice that he was required to protect Westpac's security interest, albeit that

such knowledge was already available to him by virtue of Westpac's registration and renewal of its financing statements on the Personal Property Securities Register.

[84] However, there was a more fundamental objection. I accept that Mr McKay has consistently sought information from Mr Smith regarding his trading expenses and that this has not been provided, despite Mr Smith's statutory obligation to keep and maintain that information as part of his duties in respect of the accounts and records of the liquidation[32] and his far reaching powers to obtain information regarding the Companies by way of examination or notices requiring the production of documents.[33]

[85] Mr Smith does not even state what part of the unidentifiable payments he claims are his trading expenses. This is information which he had the legal capacity to provide. Mr Smith has had in excess of a year to do so since the orders made by Fogarty J on 23 February 2015. The limited information which he did provide in his affidavit of 9 March 2015 was inadequate for any proper analysis to be made and Mr Smith chose to resist subsequent requests to provide further details. Nor did he do so in any of his 2016 affidavits. Such problem has been compounded by Mr Smith's failure to comply with his statutory reporting obligations to file reports in respect of the companies at six monthly intervals. I do not accept that Mr Smith should be entitled to rely on a failure which is entirely his own to avoid liability to pay compensation for the losses he has caused Westpac to suffer.

[86] Nor do I accept Mr Smith's proposition that Mr McKay has failed to take into account payroll expenses. The identifiable payments for which Mr McKay is not seeking recovery include those to KeyLink.

[87] Similar considerations inform my analysis of any salvage claim Mr Smith may be taken as advancing. The onus to make out such claim is on Mr Smith. He has failed to do so. In addition:

(a) Westpac never consented to the Companies being traded by Mr Smith.

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[32] Companies Act 1993, s 256.
[33] Companies Act 1993, s 305(5).

(b) There is no evidence Mr Smith's trading activities have resulted in any benefit to Westpac, such as the creation of a fund as a consequence of accounts receivable generated by Mr Smith's trading activities. I refer in that respect to Mr McKay's analysis of average weekly receipts in the pre and post-liquidation period.

(c) In any event, Mr Smith has failed to particularise which of the unidentifiable payments were paid from any such fund.

*Mr Smith's other defences*

[88] Next, Mr Smith argues that none of the assets of the Companies secured to Westpac were used by him in his trading activities. As such he appears to suggest that the proceeds of those activities were not subject to Westpac's charge. This argument is, in my view, misconceived. It is premised on the fact that seven of the Companies' trucks had a priority security to Bank of New Zealand (subsequently assigned to GFH). This is acknowledged in Fogarty J's orders. Nevertheless, Westpac had a general security over both HB and HAB at all relevant times. Therefore all assets of the Companies were secured to Westpac, albeit that seven of the trucks had a priority security. In any event, GFH's priority did not extend to any of the Companies' stock, customer lists or funds (accounts receivable or otherwise). Westpac had priority to all such assets. That priority applied to all funds of the Companies whether generated by the Companies' trading activities in liquidation or otherwise.

[89] Then, Mr Smith claims Mr McKay deliberately stopped the Companies from trading, thereby causing loss. However, that claim is factually incorrect. Mr McKay deposes and I accept that the Companies had already stopped trading before he was appointed as receiver.

[90] Mr Smith then claims that, upon Mr McKay's appointment, he "gifted for no dollars" all stock left at the depot of the landlord, the value of which Mr Smith says was $300,000. He does not provide any evidence in support of his alleged valuation.

[91] I have, in this respect, carefully considered the contents of paras [27] and [28] of Mr McKay's affidavit in reply dated 22 April 2016 and the photographs which he annexes. I am satisfied that the stock located at the premises at the time of his appointment had little or no value and that he appropriately relied on auctioneer's advice in releasing the Companies' security over the remaining stock at the premises.

[92] Mr Smith also says that Mr McKay "destroyed" the business and value of the Companies by ignoring a business sale and purchase agreement. The basis for this allegation is an affidavit by Mr H Metatangi in which he says that in 15 July 2014 his company, Global H NZ Ltd entered into a contract, conditional on due diligence, for purchase of the Companies in the amount of $420,000. After the appointment of Mr Johnson as receiver, Mr Metatangi says he was told by Mr Smith to continue his due diligence investigations via Mr Johnson. He says that he contacted Mr Johnson but did not get a reply. He then says that he heard about Mr McKay's appointment and that Mr Smith told him to contact Ms Stone. He says he left messages with her but received no response.

[93] Mr McKay and Ms Stone depose to not knowing anything about the sale and purchase agreement until Mr Smith annexed it to his first affidavit sworn on 9 March 2015. I do not regard Mr Smith's criticisms of Mr McKay as justified. I accept Mr McKay and Ms Stone's evidence that the agreement was not drawn to their attention until eight months after execution. There is no explanation as to why Mr Smith did not do so earlier. Moreover, in the event Mr Metatangi retained serious interest in the purchase he can be expected to have done more than simply leaving a message or messages with Ms Stone. There is no evidence of any written communication with Mr McKay's office about the prospective purchase or due diligence inquiries.

[94] Moreover, Mr Metatangi was required to be produced for cross-examination on his affidavit for the purposes of the resumed hearing on 10 June and did not appear.

[95] Finally, Mr Smith submits that Mr McKay failed to transfer the Companies' direct debits causing "book debts" worth $700,000 to become uncollectable. However, Mr McKay states that he never had a copy of the Companies' customer

list, the direct debit authorisation forms executed by the Companies' customers or copies of the individual contracts entered into between the Companies and their customers. He deposes that he sought that information from Mr Smith on numerous occasions but it was never provided to him. I therefore accept Mr McKay's position that he was unable to process any direct debits as he did not know who the debtors of the companies were, if those debtors had authorised the Companies to direct debit their accounts and what amount and frequency any direct debit should be.

[96] Mr Smith's affidavits also make other miscellaneous claims in the nature of a failure by Mr McKay to secure a box of stamps, that the Westpac debt "no longer exists", that Mr McKay has converted monies from Baycorp and that he generally failed to secure the assets of the Companies. I reject these allegations for the reasons Mr McKay sets out in his reply affidavit. In so far as any credibility issue arises as between Mr McKay and Mr Smith, I prefer the evidence of Mr McKay. I do so mindful particularly of the conclusions I have reached in relation to Mr Smith's purported s 305 notice.

[97] Given that Mr Smith had been debarred from defence and in order to ensure that all possible defences were properly ventilated, I also sought, subsequent to the hearing, further submissions from Mr McKay on the subject of change of position. I did so by memorandum dated 23 June 2016 and on 5 July 2016 received detailed written submissions on the point.

[98] A change of position defence is an affirmative defence[34] and as such Mr Smith was required to have pleaded it in accordance with r 5.48(4) of the High Court Rules. He did not. In any event, I am satisfied that Mr Smith could not have relied on the defence of change of position in this case as:

(a) At the time of receiving the money he knew or is deemed to have knowledge of the facts that give rise to Mr McKay's restitutionary interest, namely Westpac's position as a secured creditor of the business;

[34] *Sanders & Co v Hague* [2004] 2 NZLR 475 (HC) at [92]: A Butler (ed) *Equity and Trusts in New Zealand* (2nd ed. Brookers, Wellington, 2009) at 38.6.6(5)

(b) He did not act in good faith in that he;

- failed to acknowledge or engage with Westpac and its solicitors at the time of his appointment to determine the validity of Westpac's security;

- ignored Westpac's letter dated 13 March 2014 putting him on notice not to deal with the Companies' assets in a manner adverse to Westpac's position as a secured creditor;

- did not avail himself of his statutory right to seek directions from the Court to determine any legitimate issue as to Westpac's status as a secured creditor;

- set up two bank accounts into which he swept the accounts receivable paid into the Companies' pre-liquidation bank accounts;

- disbursed funds totalling $852,988.54 which were secured to Westpac; and

- breached his statutory duties to keep accounts and records of the liquidation, and to file six months liquidator reports, both of which would have provided details of his dealings with the funds.

(c) It is irrelevant that the money has now been spent or transferred out of Mr Smith's control.

**Result**

[99] I give judgment against Mr Smith in favour of Mr McKay in the amount of $540,402.82 together with interest on that sum calculated in accordance with the provisions of the Judicature Act 1908 from 6 August 2014, being the date of Mr McKay's appointment.

[100] In relation to costs, Mr Stewart invites consideration on the papers in due course. I reserve them accordingly.

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**Muir J**

## Schedule 1

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|---|---|---|
| 1 | “Wages”, “salaries”, payroll processing | $150,459.00 |
| 2 | “Loan repayments” | $62,523.14 |
| 3 | “Fuel” | $34,626.25 |
| 4 | Hercal Associates | $29,957.89 |
| 5 | BNZ bank charges | $14,473.45 |
| 6 | Bank Cheque | $8,474.81 |
| 7 | Rent | $2,926.00 |
| 8 | Storage Fees[35] | $2,652.67 |
| 9 | HJ Armitage | $1,600.00 |
| 10 | Vehicle testing | $1,748.68 |
| 11 | Foreign exchange transactions | $1,255.19 |
| 12 | Telephone expenses | $648.14 |
| 13 | Accommodation | $600.00 |
| 14 | Meal allowances | $300.00 |
| 15 | Interest expenses | $159.57 |
| 16 | Motor vehicle expenses | $159.20 |
| 17 | Insurance | $21.73 |
| | **Total** | **$312,585.72** |

35 Adjusted in accordance with [70] and [71] of this judgment.