2/7 (3) N2uR X

IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

7/3

B.839/81 and
B.650/82

IN THE MATTER of the Insolvency Act 1967

A N D

IN THE MATTER of the bankrupt estate of DOUGLAS JAMES GREGORY ELLIOTT

BETWEEN EXECUTIVE PRINTING (1977) LIMITED a duly incorporated company having its registered office at Auckland and carrying on business as Printers

Applicant

A N D THE OFFICIAL ASSIGNEE in the bankruptcy of DOUGLAS JAMES GREGORY ELLIOTT

Respondent

Hearing: 14th June 1984

Oral Judgment: 14th June 1984

Counsel: M C Black for applicant
Mrs M S Hinde for respondent

(ORAL) JUDGMENT OF HENRY, J.

This application contests the setting aside by the Official Assignee, pursuant to s.57(1) of the Insolvency Act 1967, of a certain mortgage No.790829.2

wherein the Applicant is mortgagee and one, Douglas James Gregory ELLIOTT, now bankrupt, is the mortgagor.

The relevant facts are not in dispute. In 1980 Elliott was indebted to the Applicant in the sum of $47,442.48 arising from guarantees by him of debentures given on behalf of certain companies which he had controlled and for which the Applicant had carried out printing work. Elliott was adjudicated bankrupt on the petition of the Commissioner of Inland Revenue and in that bankruptcy the Applicant proved the debt which I have just mentioned. There was then an application by Elliott to annul the bankruptcy, to which in due course the Applicant along with other creditors consented, the Applicant having apparently received some form of assurances as to the financial position of a further company of Elliott's, - namely Five Star Good Neighbours Limited, and his ability through the trading of that company to repay the debt. The Applicant took security by way of debenture over that other company and also by way of mortgage, being that one now in issue, over Elliott's house property. The mortgage was executed on 10 February 1981, registered on 27 May 1981 and, default having arisen under it, a power of sale was exercised with that sale being concluded on 12 July 1982. At that point of time there was owing to the Applicant a total of $52,295.42, and after payment of earlier mortgages there was left a balance of some $48,280.41.

It transpires that on 6 October 1981 a further petition had been presented against Elliott on which an order for adjudication was made on 28 April 1982. The mortgage security in issue was therefore executed within 12 months from the filing of the petition upon which Elliott was adjudicated bankrupt, and accordingly the Official Assignee applied s.57(1) of the Insolvency Act 1967, treating that mortgage as voidable. By consent of the parties, the balance of the funds to which I have referred are being held in trust pending determination of this application.

The first issue which arises is whether, under subsection (2) (a) of s.57, a situation arises so as to save the security from the operation of subsection (1). The relevant parts of subsection (2) (a) provide :

> "Subsection (1) of this section shall not affect any security or charge in so far as it relates to:
>
> (a) ... any other valuable consideration given in good faith, by the grantee of the security ... to the grantor."

It is contended for the applicant that the valuable consideration given in good faith for the

security was its consent to the annulment of the bankruptcy and also, as I understand it, to the probable or possible ability of Elliott to repay his debts by enabling him to continue trading through Five Star Good Neighbours Limited.

In my view, it is necessary to look at the real nature of the transaction in question, as the Court is instructed to do by s.5 (2) and, by doing that, to determine the real substance of that transaction. As I see it, it is only by that exercise that the Court can ascertain to what the security actually relates. The mortgage is exhibited to one of the affidavits and appears to be in standard form. It details a principal sum of $47,442.48, which is the indebtedness of Elliott to the Applicant as at that date. It required repayment on specified terms, and secures that repayment over the house property. Its real nature, in my view, can only be the securing of a past and then existing debt. There was, as I see it, no change in the nature or character of that debt arising from the giving of the security. The mere fact that the terms of the mortgage allowed payment of the principal by instalments does not, in my view, alter that character. It remained at all times a simple debt, but merely moved from being unsecured to secured. It is that debt to which the security relates. On the evidence of this transaction the security does not, in my view, relate to the consent to the annulment, which was merely

something given by the Applicant conditional upon the execution of the security. If that be so, it is probably sufficient in itself to dispose of any attack on s.57(1) and its operation.

It is, however, desirable in the circumstances to look at some of the other aspects which would arise and which have been argued in relation to s.57(2)(a). "Valuable consideration" as used in that subsection must amount to something of value, either in money or money's worth. In a recent case, not dissimilar in many respects to the present one, namely Re Austin, a Bankrupt (1982) 2 NZLR 524, Hardie Boys J. dealt with this point. In the course of his judgment (at p.528, line 39) the learned Judge said, and I quote :

> "I think it is clear that the subsection contemplates a correlation between the extent to which the security will be preserved, and the value given in exchange for the security. Such a correlation cannot be achieved except in terms of money or money's worth. The Court therefore has to put a value upon the valuable consideration, just as it must do in the case of property supplied where there is no actual price."

I respectfully agree. The consent to annulment, even if it could be said to amount to a consideration of value - and I pause here to note that an annulment is always in the discretion of the Court, and that in the instant case

there were other creditors as well as the present applicant who also consented to the annulment - it would be quite impossible here to quantify it, if indeed it has any value, and I note that the applicant has made no real attempt to do so because, of course, of the real difficulty in attempting such an exercise. As I see it all the consent was, if anything at all in this context, was a factor in allowing Five Star Good Neighbours Limited to trade and hopefully thereby enabling Elliott to pay his creditors.

In my judgment, therefore, there was here no valuable consideration given by the Applicant which was capable of quantification so as to enable subsection (2) (a) to be applied. In addition, before that subsection can operate, an Applicant must also prove that any consideration given was given in good faith. That involves posing the question: Did the applicant have good reason for suspecting that other creditors would be left unpaid? Here, on the evidence, I think the Applicant did have such good reason. Clearly at the relevant time Elliott was insolvent. He had been involved in two companies at least which had failed. There were other creditors. There would, presumably be further creditors in the future and, as I read the papers, there was no hard evidence of any continuing prosperity. The inference which I feel must be drawn is that the

Applicant got the security for the unsecured debt with the knowledge that there were other creditors, and with knowledge of at least some of Elliott's past history.

The Applicant next relies upon s.57(4)(b) of the Act, the relevant parts of which provide :

> "(4) Subsection (1) of this section shall not affect any security or charge given -
>
> (b) In substitution for an existing security or charge executed or given before the commencement of the said period:"

The existing security or charge is said to be the guarantee under the earlier debenture, or possibly the debentures themselves. A guarantee is not a security but simply constitutes a liability or a promise to pay. There was here no security given by the bankrupt but only by the companies now in liquidation by way of the debentures and which, on the evidence before me, seem to have had little if any value at the relevant time. In my opinion, the existing security referred to in subsection (4)(b) can only be an existing security given by the bankrupt. There was none such here. Neither, as I see it, was there anything in the nature of a substitution of one security for another, and accordingly this subsection can have no application.

Finally, reliance was placed on s.58 (6) which provides a code for the recovery of property, in particular where dispositions are set aside under the provisions of the Act. In my judgment, that subsection can have no application to the voidance of a security under s.57 (1). By that procedure, the Official Assignee is not seeking recovery of property from, here, the Applicant. The result of setting aside the mortgage is simply that the proceeds of sale become an asset in the bankrupt's estate. Although it is unnecessary go go into the ramifications of the application of the subsection, it seems to me to be primarily directed towards a situation where the Official Assignee is endeavouring to recover property which has found its way into the hands of some person, and where it may be equitable to give that person some relief. There are, of course, further difficulties in the way of the Applicant under this particular provision. Again, as in s.57 (2) (a), the question of good faith arises, and it seems to me that the same matters which apply in the earlier section must apply here. The consequences of that is that, on my finding, it could not be said that even if there were a receipt of property within the meaning of the subsection, that that receipt was in good faith. Moreover, as pointed out by Mrs Hinde, there is in fact no evidence of any alteration of possession by the Applicant of the nature envisaged in that provision.. Neither am I able to see anything

inequitable in the operation, in the present circumstances, of s.57 (1) so as to require the Court to alter the consequences which flow from that.

Accordingly, I find that the action of the Official Assignee under s.57 (1) were properly carried out, and that there is no relief which can be afforded the Applicant in these present proceedings. The application is therefore dismissed.

J. Henry J.

Solicitors:

Rudd, Watts & Stone, Auckland, for Applicant

Office Solicitor, Official Assignee, Auckland, for Respondent