

IN THE HIGH COURT OF NEW ZEALAND
DUNEDIN REGISTRY

CP 47/97



BETWEEN

DONALD LESLIE MITCHELL t/a D L
MITCHELL PLUMBING & DRAINAGE

Plaintiff

AND

DENNIS RUTHERFORD HESKETH

Defendant

Hearing: 11 December 1997

Judgment: 19 DEC 1997

Counsel: L A Andersen for Plaintiff
A More for Defendant

RESERVED JUDGMENT OF MASTER VENNING

The Defendant applies for orders striking out the Plaintiff's statement of claim. Alternatively the Defendant seeks an extension of time to file a statement of defence.

The Defendant was the managing director of Colonial Homes Otago Ltd (the company). On 20 May 1997 the company was put into liquidation. The Plaintiff says that the Defendant allowed the company to carry on business when it was unable to pay its creditors as they fell due, particularly during the period from July 1996 to October 1996 when the Plaintiff supplied goods and services to the sum of \$30,802.71. The Plaintiff says the Defendant was in breach of the statutory obligations contained in s135 of the Companies Act 1993, that the

Plaintiff has suffered loss and the Plaintiff accordingly seeks judgment for the \$30,802.71.

It is the Defendant's case that the relevant statutory provisions do not provide a remedy to enable the Plaintiff creditor to be compensated directly by a director and the claim should therefore be struck out.

The two relevant statutory provisions are ss135 and 301 of the Companies Act 1993. They provide as follows:

"s135 Reckless trading - A director of a company must not -

- (a) Agree to the business of the company being carried on in a manner likely to create a substantial risk of serious loss to the company's creditors; or
- (b) Cause or allow the business of the company to be carried on in a manner likely to create a substantial risk of serious loss to the company's creditors."

Section 169 provides that the duties in s135 of the Act are duties owed to the company and not to shareholders.

"s301 Power of Court to require persons to repay money or return property -

- (1) If, in the course of the liquidation of a company, it appears to the Court that a person who has taken part in the formation or promotion of the company, or a past or present director, manager, liquidator, or receiver of the company, has misapplied, or retained, or become liable or accountable for, money or property of the company, or been guilty of negligence, default, or breach of duty or trust in relation to the company, the Court may, on the application of the liquidator or a creditor or shareholder, -
 - (a) Inquire into the conduct of the promoter, director, manager, liquidator, or receiver; and
 - (b) Order that person -
 - (i) To repay or restore the money or property or any part of it with interest at a rate the Court thinks just; or
 - (ii) To contribute such sum to the assets of the company by way of compensation as the Court thinks just; or
 - (c) Where the application is made by a creditor, order that person to pay or transfer the money or property or any part of it with interest at a rate the Court thinks just to the creditor.

- (2) This section has effect even though the conduct may constitute an offence.
- (3) An order for payment of money under this section is deemed to be a final judgment within the meaning of section 19(d) of the Insolvency Act 1967.”

Section 301 is, with the exception of subs(1)(c) and the ability of the creditor to make the application, in broadly similar terms to the former s321 of the Companies Act 1955.

The Plaintiff issued proceedings earlier this year against the Defendant in the District Court at Dunedin claiming identical relief. Those proceedings were issued prior to the liquidation of the company. It is apparent there was no jurisdiction for the application under s301 prior to the liquidation of the company. The proceedings were dismissed. The former proceedings are no bar to the present proceedings.

Section 301 clearly contemplates that an application may be made to the Court by a creditor. In the present case the creditor has made application to the Court and seeks relief directly against the Defendant. The Plaintiff does so in reliance upon s301(1)(c)

At issue is the construction of s301. Neither counsel were able to find any authority on the point.

A number of elements are contained in s301. They include:

- (i) The section applies in the course of a liquidation;
- (ii) Application to the Court may be made by a liquidator, creditor or shareholder;
- (iii) The Court may make certain orders against named persons, in this case a director, in the following circumstances:
 - (a) where the director has misapplied, or retained, or become liable or accountable for, money or property of the company; or

- (b) been guilty of negligence, default or breach of duty or trust in relation to the company.
- (iv) The Court may inquire into the conduct of the director; and
- (v) Order the director to repay or restore the money or property or to contribute such sum to the assets of the company by way of compensation.

There are thus two circumstances identified in the body of s301(1) where orders may be made. The first circumstance is where the director owes a specific item of money or property to the company, and the second circumstance is where the director has breached his duties to the company and caused loss generally to the company.

It follows in my view as a matter of construction that the reference to restoring *the money or property or any part of it* in s301(1)(b)(i) is a reference back to the first circumstance. The reference to the “money or property” and “repay or restore” are consistent with such an interpretation. the more general option of contributing *such sum to the assets of the company* under s301(1)(b)(ii) is consistent with the second circumstance where general damage has been caused to the company. An assessment of the damage is required to be made by the Court and an order that the director contribute such sum to compensate for the damage can then be made. The reference to “such sum” in s301(1)(b)(ii) is not to an identifiable or specific sum, but to the sum assessed by the Court by way of compensation.

Against that background s301(1)(c) falls to be considered. It provides that where the application to the Court is made by a creditor the Court may order the director to pay or transfer *the money or property or any part of it* to the creditor. The irresistible inference is that the reference to “the money or property” is a reference back to the money or property identified in the first circumstance in the main body of s301(1) and repeated in s301(1)(b)(i). No provision is made in s301(1)(c) for the Court to order a payment by the director to

the creditor of any part of the general damages sum that may otherwise be ordered under s301(1)(b)(ii).

Mr Andersen submitted that because the remedy in s301(1)(c) is additional to the remedy in s301(1)(b) it can only relate to the situation where the Defendant has been guilty of negligence, default or breach of duty or trust in relation to the company as the other breaches require the property in question to be restored to the company. With respect to that submission, however, in my view it is contrary to the clear wording of the subsection.

Alternatively Mr Andersen submitted that having regard to s5(j) of the Acts Interpretation Act 1924 a fair, large and liberal construction interpretation should be given to the section. The difficulty with that is that the wording of s301(1)(c) is in my view clear. It limits the circumstances in which a creditor may recover directly from the director to the first circumstance. That cannot be overcome by application of s5(j)

The interpretation argued for by the Plaintiff could be advanced if the section could be interpreted as establishing a three stage process. The first stage is the inquiry. The second stage is an order that the director either repay or restore the money or property or contribute such sum to the assets of the company as fixed by the Court, thereby in either case putting the company in funds. The third stage of the process is then the direction that a payment be made to the creditor. On that analysis the money or property referred to in s301(1)(c) could be the money recovered by the company under either of the legs in s301(1)(b).

However, in my view such an interpretation can not be sustained for two reasons. First, the inclusion of the additional "or" at the conclusion of s301(1)(b)(ii), and secondly s301(1)(c) provides for an order that the director pay or transfer the money or property directly to the creditor rather than the money recovered by the company be paid to the creditor.

I find therefore that a creditor cannot rely upon s301(1)(c) to recover directly from a director in the second circumstance where the director has been guilty of negligence, default or breach of duty or trust in relation to the company. In this case the Plaintiff relies upon a breach of s135 of the Act which is clearly within the second circumstance. The Plaintiff is not entitled to recover directly from the director.

However, I accept Mr Andersen's submission that, even if that is so, the proceedings should not be struck out. Clearly the application may be made to the Court by a creditor in the second circumstance as well as in the first circumstance, but in such a case the application is effectively for the benefit of all creditors. The relief sought may have to be amended, but the creditor is still entitled to pursue the application. The proceeding is clearly capable of amendment: *Marshall Futures v Marshall* [1992] 1 NZLR 316.

In light of the above finding the creditor may well wish to discuss the proceedings with the liquidator to ascertain whether the liquidator will bring proceedings on behalf of all creditors. The creditor may also wish to consider his position as to whether he is prepared to continue with the proceedings in their current form for the benefit of all creditors.

Summary

To enable the Plaintiff time to consider his position and, if necessary, to file an amended statement of claim the application to strike out is adjourned for call on 4 March 1998 upon terms:

- (a) Any amended statement of claim is to be filed by 20 February 1998.
- (b) If the amended statement of claim is not filed by 20 February 1998 the proceedings will be struck out with the issue of costs to be dealt within on 4 March 1998.

- (c) If an amended statement of claim is filed by 20 February 1998 this application to dismiss will itself be dismissed with costs to be dealt with on 4 March 1998.

Procedure

An application by a creditor under s301 raises certain procedural issues. The application is an application for relief under s301 of the Companies Act 1993. As such it is an application which should be brought by way of proceedings under Part IV of the Act: R448(1)(c). Clearly a liquidator may be interested in the proceedings where they are brought by one creditor. The liquidator is not a party to the proceedings. As a matter of course the proceeding does not require directions as to service as R451(1)(c)(b) provides:

“Where the proceeding is under the Companies Act 1993 and is not a proceeding in the liquidation of a company or a proceeding under s174 of the Act: ... the plaintiff shall apply to the Court ex parte for directions as to service and for such orders for representation as may be required.”

In this case the application clearly is a proceeding in the liquidation of a company and so prima facie directions as to service are not required.

As counsel did not address on this issue I leave the question of the procedure open. I invite counsel for the Plaintiff to consider whether an application for directions as to service should be made under R451(1)(b) if the matter is to proceed.


MASTER VENNING

Solicitors:
Calvert & Co, Dunedin for Plaintiff
O'Neill Devereux, Dunedin for Defendant