IN THE HIGH COURT OF NEW ZEALAND
NAPIER REGISTRY

CIV 2008-441-37

IN THE MATTER OF	TENNYSON BM LIMITED (in liquidation)
BETWEEN	JOHN RICHARD PALAIRET AND DAVID WILLIAM PEARSON Plaintiffs
AND	TURBO ASSOCIATES LIMITED Defendant

Hearing: 27 March 2009

Appearances: D. Chan - Counsel for Plaintiff
N. Gray - Counsel for Defendant

Judgment: 24 April 2009 at 3.00 pm

JUDGMENT OF ASSOCIATE JUDGE D.I. GENDALL

This judgment was delivered by Associate Judge Gendall on 24 April 2009 at 3.00 p.m. pursuant to r 11.5 of the High Court Rules.

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Introduction

[1] Before the Court is an application by the liquidators of Tennyson BM Limited (in liquidation) ('the Company') to set aside a transaction under sections 292 and 294 of the Companies Act 1993 ('the Act'). Alternatively, they seek to recover the value of goods transferred in the transaction under section 298 of the Act.

[2] The transaction in question involved the transfer of the Company's Manukau restaurant plant and chattels valued at $51,734.00 ("the goods") from the Company to the defendant company, Turbo Associates Limited ('Turbo').

[3] Turbo opposes the applications.

Background Facts

[4] The Company (formerly known as Breakers Manukau Limited) operated a restaurant in Manukau and used the goods in this operation. It was part of a group of companies ('the TIG Group') whose parent company was Turbo Investments Group Limited (not to be confused with the defendant, Turbo Associates Limited). On 12 April 2006 the Company gave security over all of its assets to ANZ Bank by way of a General Security Agreement.

[5] In early 2007 it is said that the TIG Group identified a need for further capital, and developed a general restructuring plan with the support of ANZ Bank. A financial analysis of the Company and other companies in the TIG Group was undertaken, and on 16 August 2007 it was decided that the Company would cease trading from that day.

[6] Turbo was incorporated on 30 August 2007 as part of the restructuring plan. On 14 September 2007 Turbo agreed to purchase certain assets from Turbo Investments Group Limited and to become responsible for certain liabilities. To ensure the ANZ Bank's overall security interests were not prejudiced, Turbo entered into a General Security Agreement securing in favour of ANZ Bank the total debt of the restructured group, now known as the Turbo Associates Limited Group ('the TAL Group').

[7] The defendant, Turbo, states that part of the restructuring plan was that the goods owned by the Company would be used by another company in the Group that also operated as a restaurant. Turbo says that on 16 August 2007 it was agreed in principle that the goods owned by the Company would be transferred to it.

Implementation of that agreement was to take place at a later date, as the parties were apparently awaiting a valuation report for the goods which did not arrive until 16 January 2008.

[8] On 16 January 2008 this independent valuation valued the goods at $51,734.00. The 4 December 2008 affidavit of Mr. Bruce McCallum, director of Turbo filed in this proceeding contends that as the Company had ceased business the market value of the goods if sold on a normal break-up basis would have been considerably less than this $51,734.00 figure. He deposes that as it was believed the goods could be legitimately transferred to a Group company, Turbo was content with the higher figure.

[9] The formal agreement for the transfer of goods from the Company to Turbo was entered into on 26 February 2008. The agreement refers to payment for the goods by way of part satisfaction of an inter-company debt in the amount of $51,734.00, plus a cash payment to cover the GST involved. The agreement records the "Effective Date" of the transaction as 31 August 2007.

[10] The defendant Turbo contends however that the agreement does not accurately reflect what actually took place, and that there has never been a debt owed by the Company to Turbo. As such, the transfer was not paid for by way of satisfaction of inter-company debt. The economic reality, as suggested by the defendant, is that Turbo acquired the goods along with a liability to ANZ Bank for the value of the goods.

[11] On 27 February 2008 the Company was put into liquidation by the High Court in Napier.

[12] On 4 November 2008 the plaintiff liquidators filed an application for orders under sections 292 and 294 of the Act to set aside the transaction. This was amended on 22 January 2009 to include an alternative claim under section 298 of the Act.

Companies Act 1993

[13] Section 292 provides as relevant:

> **"292 Insolvent transaction voidable**
> (1) A transaction by a company is voidable by the liquidator if it—
> (a) is an insolvent transaction; and
> (b) is entered into within the specified period.
> (2) An insolvent transaction is a transaction by a company that—
> (a) is entered into at a time when the company is unable to pay its due debts; and

(b) enables another person to receive more towards satisfaction of a debt owed by the company than the person would receive, or would be likely to receive, in the company's liquidation.

(3) In this section, transaction means any of the following steps by the company:

(a) conveying or transferring the company's property:

…

(4A) A transaction that is entered into within the restricted period is presumed, unless the contrary is proved, to be entered into at a time when the company is unable to pay its due debts.

…

(5) For the purposes of [subsections (1) and (4B), specified period means—

(a) The period of 2 years before the date of commencement of the liquidation together with the period commencing on that date and ending at the time at which the liquidator is appointed; and

(b) In the case of a company that was put into liquidation by the Court, the period of 2 years before the making of the application to the Court together with the period commencing on the date of the making of that application and ending on the date on which[, and at the time at which,] the order was made[; and]

(c) If—

(i) An application was made to the Court to put a company into liquidation; and

(ii) After the making of the application to the Court a liquidator was appointed under paragraph (a) or paragraph (b) of section 241(2),—

the period of 2 years before the making of the application to the Court together with the period commencing on the date of the making of that application and ending on the date [[and at the time]] of the commencement of the liquidation.]

(6) For the purposes of [subsection (4A), restricted period means—

…

(b) In the case of a company that was put into liquidation by the Court, the period of 6 months before the making of the application to the Court together with the period commencing on the date of the making of that application and ending on the date on which[, and at the time at which,] the order of the Court was made[; and]

…".

[14] Section 294 sets out the procedure liquidators must follow to have a transaction set aside under section 292.

[15] Section 298 provides as relevant:

"298 Transactions for inadequate or excessive consideration with directors and certain other persons

…

(2) Where, within the specified period, a company has disposed of a business or property, or provided services, or issued shares, to—

…

(c) Another company that was, at the time of the disposition, provision, or issue, controlled by a director of the company, or a nominee or relative of or a trustee for, or a trustee for a relative of, a director of the company; or

(d) Another company that, at the time of the disposition, provision, or issue, was a related company,—

the liquidator may recover from the person, relative, company, or related company, as the case may be, any amount by which the value of the business, property, or services, or the value of the shares, at the time of the disposition,

provision, or issue exceeded the value of any consideration received by the company.

…

(4) For the purposes of subsections (1) and (2) of this section, specified period means—

(a) The period of 3 years before the date of commencement of the liquidation together with the period commencing on that date and ending at the time at which the liquidator is appointed; and]

(b) In the case of a company that was put into liquidation by the Court, the period of 3 years before the making of the application to the Court together with the period commencing on the date of the making of the application and ending on the date on which[, and at the time at which,] the order of the Court was made[; and]

(c) If—

(i) An application was made to the Court to put a company into liquidation; and

(ii) After the making of the application to the Court a liquidator was appointed under paragraph (a) or paragraph (b) of section 241(2),—

the period of 3 years before the making of the application to the Court together with the period commencing on the date of the making of that application and ending on the date [[and at the time]] of the commencement of the liquidation."

The Issues

[16] The liquidator argues that, pursuant to section 292 of the Act, the transaction to transfer the goods from the Company to Turbo was an insolvent transaction. They contend that it was entered into on 26 February 2008, at which time the Company was unable to pay its due debts and that it enabled Turbo to receive more towards satisfaction of a debt owed by the Company than Turbo would have been likely to receive in the Company's liquidation. The liquidator denies that the transaction was entered into on 31 August 2007, but state that, in any event, the Company was also unable to pay its due debts on that date.

[17] Turbo asserts first, that the transaction was entered into on 31 August 2007, at which time the Company was able to pay its debts. Turbo denies that the transaction enabled it to receive more towards satisfaction of a debt than would have been likely in liquidation, as it insists now that no debt was owed to Turbo by the Company. Turbo further states that it did not receive a benefit which would have been available to the liquidator, as proceeds from the goods in question would always be paid to ANZ Bank in light of their secured interest.

[18] As I see it, the issues pertaining to the section 292 application are:

a) What is the date of the transaction, and was the Company able to pay its due debts at that date?

b) Was the transfer of assets towards satisfaction of a debt owed by the Company to Turbo?

c) Was Turbo preferenced by the transaction pursuant to section 292(2)(b)?

[19] The plaintiff liquidators argue in the alternative that, if Turbo was not a creditor of the Company, and the goods were not received in partial satisfaction of debt, then the goods were transferred to Turbo with the Company receiving nothing in return. As such, disposition of the goods was for inadequate consideration and is caught by section 298.

[20] Turbo argues in response that the disposition was for good consideration in that in taking on the goods, Turbo also took on a liability to ANZ Bank for the exact value of the goods.

Section 292 application

Could the Company pay its due debts at the time of the transaction?

[21] The date on which the transaction was entered into is a matter of dispute between the parties. However, there is no dispute that the transaction was entered into within the restricted period as defined in subsection (6) of section 292. As such, pursuant to subsection (4A), it is presumed that the transaction was entered into at a time when the Company was unable to pay its due debts. The onus is then on the defendant Turbo to rebut this presumption.

[22] The plaintiff liquidators argue that the transaction was entered into on 26 February 2008. This being the day before liquidation, it is more likely the Company was unable to pay its due debts at this date than the defendant's contended date of 31 August 2007.

[23] It was argued for the defendant, Turbo, that 31 August 2007 is the appropriate date, as that was the day after the defendant was incorporated, and immediately after the defendant and the Company agreed to proceed with the transaction. The delay between that time and the formal documentation of the agreement being completed on 26 February 2008 was simply due to delay in receiving the independent valuation of the goods.

[24] The plaintiff liquidators contend that the sale could not have occurred at this date, as the price was not determined by the valuation until 16 January 2008.

Furthermore, the goods were encumbered by the General Security Agreement in favour of ANZ Bank and the Bank did not give its consent to the transfer until 26 February 2008. The alleged repayment of debt (although the defendant, Turbo, now denies that there was any repayment of debt at all) was not recorded in the Company's general ledger until 29 February 2008.

[25] In response, the defendant, Turbo, maintains that the parties intended the encumbered title in the goods to pass unconditionally on 31 August 2007, at a price to be fixed by the valuation – s. 19 Sale of Goods Act 1908. Turbo characterises the formal agreement of 26 February 2008 as merely settlement for the transaction by which title in the goods had already passed as at 31 August 2007.

[26] The parties, it seems, provisionally agreed at or around 31 August 2007 to convey the goods to the defendant as part of the wider restructuring process. However, in my view, it is difficult for the defendant Turbo to say that the parties intended the encumbered title in the goods to pass unconditionally at that date, when first, the parties knew that the consent of the ANZ Bank was required under the General Security Agreement before a sale could take place, and secondly, when all this occurred in circumstances where those involved expressed the utmost concern that any transfer was with ANZ Bank's consent and did not prejudice ANZ Bank's interests (In this regard, I refer to the affidavit of Mr Nigel Boyd Foster, interim CEO of Turbo Investments Group Limited, dated 4 March 2009, paras 10-11; and the affidavit of Mr. Bruce McCallum dated 4 December 2008, paras 7, 16).

[27] As such, I find that the relevant date of the transaction is 26 February 2008. The defendant has not discharged the onus of showing that the Company was able to pay its due debts at this date, and, being the day before the Company was placed into liquidation, I have no doubt that the Company was not able to pay its due debts at this date.

Was the transaction in satisfaction of a debt?

[28] The agreement for sale and purchase of the goods states explicitly at clause 4 that payment for the goods is:

> "as to the sum of $51,734.00 by the buyer accepting the Goods in part satisfaction of an inter-company debt owing by the seller to the buyer…"

[29] On 29 February 2008 an entry was made in the Company's general ledger showing a reduction of $58,200.75 in inter-company debt owed by the Company.

[30] The defendant now argues that these references to inter-company debt are the result of human error, and that in fact the Company did not owe any such debt to the defendant. This explanation is rejected by the plaintiffs.

[31] Mr. Nigel Foster in his affidavit, paragraph 12, explains the alleged error as follows:

> "I believe the reason I, company management, and the company's advisors did not pick up on the error was because the method of transfer was not the main focus of attention. The main consideration was that [the Company] acted lawfully in the transfer of its goods and that the party entitled to those goods or any proceeds from them would in fact receive them. That party was ANZ and not any other party, including a liquidator of [the Company]."

[32] Mr. Bruce McCallum in his 4 December 2008 affidavit at paragraph 21 explains as follows:

> "The transfer of the Goods from [the Company] to [Turbo] was the last step in a number of transactions involving the TAL Group and the TIG Group Companies. The process had been time consuming, costly and with a number of conditions to be satisfied by a number of parties. This was on top of a small group in management having to cope with a number of operational matters in companies that had some financial stress. This is the reason for the agreement not correctly describing what in fact was taking place."

[33] He further states at paragraph 15 of this affidavit that the defendant could not have been a creditor of the Company, as the defendant was incorporated after the Company ceased trading.

[34] The plaintiff Mr. John Palairet notes at paragraph 17 of his 23 January 2009 affidavit that Mr. Bruce McCallum and another director signed the Agreement, and that he is not aware of any documents which support Mr McCallum's contention that the Agreement is incorrect or misrepresents the true position.

[35] Despite the insistence in his affidavit evidence that the defendant was never a creditor of the Company, Mr. Bruce McCallum in cross-examination before me appeared to accept that the debt owed by the Company to Turbo Investments Group was part of the sale of Turbo Investments Group's assets to the defendant. It was

accepted that the debt owed was around $800,000.00, but it was said it had a market value of nil:

> "A. I believed then and I believe now that the debt had no value to me and that amounted to the debt not transferring.
>
> …
>
> Q. The value of the debt in the sense of whether it is recovered might be zero. But the debt itself remained exactly the same amount. Didn't it. Between [the Company] and [Turbo Investments Group].
>
> A. Yes
>
> Q. And that was transferred to Turbo as part of the assets?
>
> A. In accordance with the Sept agreement it would appear so."

[36] In light of the above evidence, I find that the defendant, Turbo, was in fact a creditor of the Company: *Gray v Chilton Saint James School* (1997) 8 NZCLC 261,306. The issue then remains as to whether the transfer of assets in this particular transaction went towards the satisfaction of debt owed by the Company. The contract for the transaction and the entry in the Company's general ledger both suggest that this is the case.

[37] The plaintiff liquidators argue that if the transfer of assets was not in satisfaction of debt owed, then the defendant gave no consideration for the assets. The defendant however seems to suggest that the consideration was the taking on of the Company's liability to ANZ Bank of an amount representing the value of the goods, so that the defendant received $51,734.00 worth of assets set against a further $51,734.00 in liability to ANZ Bank. While this argument on its face seems plausible, it appears that part of the restructuring arrangement for the group of companies was that the defendant, Turbo, would take on liability for the entire debt of the whole group to ANZ Bank anyway. This was also alluded to before me in the cross-examination of Mr. Bruce McCallum:

> "Q. So you are saying that the consideration in your mind at the time you signed was taking on the liability.
>
> A. Yes.
>
> Q And reducing inter-company debt.
>
> A. No the principle consideration in my mind at all times in respect of this transaction and all of the other transactions undertaken as part of the restructuring were subject to the ANZ Bank's security. We were in a position where we could not carry out the restructuring without the full support of the ANZ Bank and that was my principal focus at all times.
>
> Q. Did Turbo take on responsibility of the entire group debt?

> A. Yes it did, it contracted the ANZ group wide facility.
>
> Q. So it was taking on that liability anyway.
>
> A. It was taking on that liability and all of the assets which were secured by the facility. That is why all companies in the group were subject to the cross-guarantees."

[38] As I see the overall position, both the agreement for the transfer of the goods and the entry in the Company's general register clearly indicate that the transfer of those goods was in satisfaction of an inter-company debt. In my view, prima facie this establishes that the transfer was indeed in satisfaction of this debt. Submissions advanced on behalf of the defendant, Turbo, suggesting that this was in error, and that the consideration was in fact the taking on of liability to ANZ Bank, submissions which are not supported by any independent documentary evidence, in my view are insufficient to rebut what the contract and general register clearly show.

Was Turbo preferred by the transaction?

[39] The defendant, Turbo, further suggests that the transaction does not fall within section 292, as the transaction did not diminish the pool of assets available for distribution amongst the creditors, which is the policy behind the provision: *Re Modern Terrazzo Ltd (in liq)* [1998] 1 NZLR 160. It states that as the goods were subject to ANZ Bank's security, the goods or their monies worth were never going to be available to the general pool of creditors. If the goods were not transferred to the defendant, Turbo, they would have been sold with the proceeds of sale going to ANZ Bank. While there is no direct evidence of the debt owed to ANZ Bank before me, the affidavit evidence of Mr. Bruce McCallum suggests that for the entire group it was over $6 million. This being far more than the value of the goods, the other creditors of the Company would not have received any of the proceeds. As such, Turbo's argument is that the creditors were not disadvantaged in any way by the transfer of the assets to it.

[40] In response, the plaintiff liquidators argue that this is the wrong test. They state that the question under section 292 is not whether they would have received the money if there had been a different kind of transaction, but simply whether the transaction enabled the defendant, Turbo, to receive more towards the satisfaction of its debt than Turbo would have received in the liquidation.

[41] In *National Bank of New Zealand v Coyle* (1999) 8 NZCLC 262,100 a similar argument was raised to the effect that the focus of the insolvent transaction provisions

is no longer on the dissipation of a company's assets available to the general body of creditors, but only on whether the particular creditor received more than would have been likely in liquidation. This was rejected by Pankhurst J however:

> "For the Liquidator it was argued that s 292 effected a fundamental shift in that dissipation of the assets of the Company available to the general body of creditors was no longer important, rather the issue was whether the particular creditor had received more than would have been likely in the liquidation.
> …
> Unquestionably the old test of subjective intention to prefer has been caste [sic] aside in favour of an inquiry concerning whether the creditor has likely received more than would have been the case in the liquidation. But does this mean that the underlying philosophy of the section has also changed: that the absence of dissipation of assets and thereby harm to the general body of creditors, is no longer required? I doubt it. As recently as 1997, albeit with reference to the voidable preference section in the 1955 Companies Act, the Privy Council in Lewis v Hyde [1998] 1 NZLR 12 referred to the "universal assumption" that an actual preference was required…
> I am of the view that this reasoning is still of equal application. <u>The voidable transaction regime is based on the premise that the general body of creditors has been disadvantaged as a result of the treatment afforded one of their number. In the absence of detriment I do not think there is a basis for the Liquidator to intervene and set aside a transaction."</u> (my emphasis)

[42] Bearing these matters in mind I now turn to consider whether Turbo was preferred by the transaction in question here. As I have noted above, I have found that the defendant, Turbo, was a creditor of the company, that the $51,734.00 worth of goods were exchanged for a reduction in debt owed by the company to Turbo and it is clearly apparent from the statement of affairs of the company in liquidation that the defendant, Turbo, did receive more towards the satisfaction of its debt then would otherwise have been received in the liquidation.

[43] Alternatively, turning to the test outlined by Pankhurst J. in *National Bank of New Zealand v Coyle*, I am satisfied here that the general body of creditors of the company has been detrimentally effected and disadvantaged as a result of the treatment afforded to Turbo by the transfer of the goods to it.

[44] The ANZ Bank chose to release its General Security Agreement over these goods. That was a matter for it. And, even if the bank here remained as an unsecured creditor of the company along with Turbo and its other creditors, if this transaction had not taken place, the value of the goods would have been available to the liquidator and all creditors would have shared in them on a *pari passu* basis, a classic concern of our long-standing voidable preference principles. The whole timing of this transaction

immediately prior to liquidation of the company and the clearly documented transfer of the goods in exchange for debt reduction owed by the company clearly points to the fact that the transaction here is objectionable in the sense that the company as a debtor has partly satisfied the claims of just one (closely related) creditor company at a time when it lacked sufficient assets to satisfy its legitimate obligations to other creditors. Turbo took the goods at an agreed valuation price and made use of these in another restaurant owned by a member of the group. Prior to the goods leaving the ownership of the company, as I understand the position, a release of the ANZ Bank security held over them was arranged. On settlement, it was only the debt owing by the company to Turbo which was reduced and the general body of creditors of the company, as a result, was disadvantaged.

[45] I conclude therefore that in terms of ss. 292 and 294 of the Act the plaintiff liquidators have been successful in making out the required grounds to set aside the transaction as a voidable one.

[46] That said, the plaintiffs' liquidator's application before me succeeds.

[47] The goods, however, have been transferred to Turbo. I am told that Turbo has provided its own security over the goods to a third party, the ANZ Bank. Before me, Mr Chan for the liquidators indicated that the liquidators do not seek the return of the goods. Instead they seek an order effectively under s. 295(c) of the Act that Turbo pay to the company the value of the goods totalling $51,734.00.

[48] Section. 295(c) of the Act states:

> "If a transaction or charge is set aside under s. 294, the Court may make one or more of the following orders:
>
> (a) an order that a person pay to the company an amount that, in the Court's opinion, fairly represents some or all of the benefits that the person has received because of the transaction ".

[49] The $51,734.00 represents the amount which under the contract between them, the company and Turbo agreed was to be paid (by debt reduction) for the transfer of the goods. Mr Gray for Turbo suggests this is an inflated figure and not the true value of the goods here. I reject this argument. Although the valuation of the goods may

have been undertaken on the basis that they were sold as a going concern, Turbo itself confirms that the goods were used by it in one of the group's other restaurants, no doubt on a going concern basis. I accept therefore that the benefit received by Turbo as a result of this transaction was $51,734.00 representing the valuation figure for the goods.

[50] Section 296(1) of the Act indicates here that the new security interest the ANZ Bank has provided by Turbo over the goods subsequent to their acquisition from the company is not to be affected by the setting aside of the transaction. That said, in my view, therefore an appropriate remedy for the plaintiff liquidators is for the order they seek under s. 295(c) of the Act to be made. That order is to follow.

[51] This effectively disposes of the application by the plaintiff liquidators which is before the Court. Turning briefly to the alternative claim by the plaintiffs under s. 298 of the Act, given my finding that the $51,734.00 consideration for the goods provided by Turbo was fully applied in reduction of the company's debt as the parties clearly set out in the contract between them, it cannot be said that the disposition exceeded the consideration received here by the company. As such, there can be no recovery by the plaintiff liquidators of any amount under s. 298 of the Act.

Result

[52] The application by the plaintiff liquidators pursuant to ss 292 and 294 of the Act succeeds.

[53] An order is now made requiring the defendant, Turbo, to pay to the company Tennyson BM Limited (in liquidation) within 20 working days of the date of this judgment the sum of $51,734.00 in terms of s. 295(c) of the Act.

[54] As to costs on this proceeding, these are reserved. If counsel are unable to agree between themselves on the issue of costs then they may file costs memoranda sequentially and in the absence of either counsel indicating they wish to be heard on the matter, I will decide the question of costs based upon the material filed.

'Associate Judge D.I. Gendall'