IN THE HIGH COURT OF NEW ZEALAND
PALMERSTON NORTH REGISTRY

CIV-2008-454-940

IN THE MATTER OF	the Companies Act 1993
BETWEEN	THE COMMISSIONER OF INLAND REVENUE Plaintiff
AND	AOTEAROA COOLSTORES LIMITED Defendant

Hearing: 1 October 2009

Appearances: P. Latimer - Counsel for Plaintiff
M. Ryan - Counsel for Defendant
P. Drummond - Counsel for Creditors in Support, Jones Refrigeration Limited and Anthony Refrigeration Limited
R. Oakley - Counsel for a Creditor in Support, James Bull Holdings Limited

Judgment: 5 October 2009 at 3.30 pm

JUDGMENT OF ASSOCIATE JUDGE D.I. GENDALL

This judgment was delivered by Associate Judge Gendall on 5 October 2009 at 3.30 p.m. pursuant to r 11.5 of the High Court Rules.

Solicitors: Inland Revenue Department, PO Box 1462, Wellington
M.B. Ryan, Solicitors, PO Box 12054, Palmerston North

[1] This is an application by the plaintiff seeking an order to place the defendant company into liquidation. It is opposed by the defendant.

Creditors in Support

[2] At the outset Mr. Drummond, counsel for creditors in support Jones Refrigeration Limited and Anthony Refrigeration Services Limited noted that the debts owing to those parties had been settled and they sought leave to withdraw from this proceeding as creditors in support.

[3] At the hearing on 1 October 2009, leave was granted accordingly and I now confirm this.

[4] On questions of costs, so far as Anthony Refrigeration Services Limited was concerned, Mr. Drummond confirmed that there was no issue as to costs. With regard to Jones Refrigeration Limited, however, although the debt owing to that creditor had been settled, costs were sought with respect to its appearance as a creditor in support.

[5] Having heard counsels' submissions, at the hearing, costs calculated on a Category 2B basis together with disbursements (if any), as approved by the Registrar were awarded to Jones Refrigeration Limited as a creditor in support.

[6] Also at the outset Ms. Oakley appeared for James Bull Holdings Limited, a further creditor in support and indicated that the debt owing to that company had been settled and it was seeking leave to withdraw.

[7] Leave to withdraw as a creditor in support was granted to James Bull Holdings Limited and I now confirm this. On the question of costs, Ms. Oakley confirmed that there was no issue as to costs relating to James Bull Holdings Limited.

[8] This left the original appearances in support of the liquidation application filed by the following creditors:

(a) By Fitzherbert Rowe claiming 9,089.86 filed on 4 February 2009;

(b) By Lion in the Sun NZ Limited claiming $8,513.54 filed on 25 June 2009; and

(c) By Red Consulting Group Hawkes Bay Limited claiming $12,585.95 filed on 8 July 2009.

[9] In addition, on 17 September 2009, Visy Board (NZ) Limited, also filed an appearance as a further creditor in support of the present application, noting a debt due of $41,709.38.

[10] I now turn to the substantive application before the Court.

Liquidation Application

[11] In its present claim the plaintiff, as I have noted, is seeking an order that the defendant company be placed into liquidation. On 6 November 2008 the plaintiff served upon the defendant a statutory demand claiming the sum of $809,359.99 said to be for outstanding PAYE, Kiwi Saver Employee Deductions, Kiwi Saver Employer Contributions, Student Loan Repayment Deductions, Goods and Services Tax and Income Tax.

[12] The defendant did not pay the amount demanded within the 15 working day period specified in the statutory demand, nor did the defendant apply to set-aside the statutory demand.

[13] A statutory presumption of insolvency on the part of the defendant therefore arose in terms of s. 287 Companies Act 1993. Subsequently, on 18 December 2008 the plaintiff filed its statement of claim in this proceeding seeking an order that the defendant be placed into liquidation in reliance on this presumption of insolvency.

[14] Advertising of the proceeding, however, did not take place until 9 July 2009 (in the New Zealand Gazette) and 15 July 2009 (in the Manawatu Standard newspaper).

[15] The matter had been called before this Court in the mean time on 9 February 2009, 2 March 2009, 11 May 2009 and 23 July 2009 and then it was again called on 20 August 2009 and 21 August 2009.

[16] By the time the call on 21 August 2009 took place, it is clear that the defendant company had managed to make several payments to the plaintiff which, with a final payment on 21 August 2009, had cleared the $809,359.99 debt in the statutory demand entirely.

[17] In the mean time, however, a substantial additional tax liability had accrued due from the defendant. On 21 August 2009, Mr. Latimer for the plaintiff provided a solicitor's certificate to the Court indicating that the defendant's outstanding debt then owing to the plaintiff was $2,022,658.51, although this was modified in a solicitor's certificate provided on 1 October 2009 to a total outstanding debt of $1,308,325.77. In addition, at the call of this matter on 21 August 2009 Mr. Latimer for the plaintiff sought an order from this Court placing the defendant company into liquidation.

[18] Following the 21 August 2009 call of the matter, I gave a judgment on 27 August 2009 which adjourned the liquidation application to 1 October 2009 and in so doing made the following directions:

> "[34] Leave is granted to the defendant to file and serve its statement of defence to the plaintiff's application out of time. A direction is made that this statement of defence is to be filed and served within 5 working days of today (27 August 2009).
>
> [35] A further direction is made that the defendant is to file and serve detailed affidavit evidence as to its solvency or otherwise for consideration by the Court within 15 working days of today (27 August 2009).
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> [36] The plaintiff is to have a period of a further 5 working days from that date to file and serve any affidavit evidence in reply."

[19] The reasons given in that 27 August 2009 judgment for acceding to the defendant's request for a further adjournment were set out at para. [32] in the following way:

> "[32] Weighing up all these considerations and under the circumstances prevailing here, I am satisfied that a further short adjournment of this matter to allow the defendant an opportunity to provide the Court with detailed and independent verification of its solvency both on the basis of its asset and liability position and the 'cash flow' test is in the best interests of justice here. This will enable the Court to have all the available evidence before it when considering and making a proper decision on the present application."

[20] On 3 September 2009 the defendant filed its statement of defence. On 18 September 2009 it filed a second affidavit of Kenneth William Thurston ("Mr. Thurston") in support of its opposition to the liquidation application.

[21] In response, on 25 September 2009 the plaintiff filed a reply affidavit of Rohan Enoch Light ("Mr. Light"). And, at the commencement of the 1 October 2009 hearing before me, Mr. Ryan for the defendant sought leave to file and have read a further third affidavit of Mr. Thurston sworn earlier that day.

[22] Although Mr. Latimer for the plaintiff initially and properly objected to the last minute filing of Mr. Thurston's 1 October 2009 affidavit, he expressed the view that matters in the affidavit were not relevant to the issues before the Court and in any event they would not require a response from the plaintiff. Given this and the need as I saw it for the Court to have all the available evidence before it to properly consider the plaintiff's liquidation application, I granted leave for the late filing of this 1 October 2009 affidavit of Mr. Thurston and ruled that it would be read as part of a consideration of the application before the Court.

Counsels' Arguments and My Decision

[23] The present liquidation application is brought pursuant to s. 241(4)(a) Companies Act 1993. This provision allows the Court to appoint a liquidator if it is satisfied that the company in question is "unable to pay its debts".

[24] As I have noted above, s. 287 Companies Act 1993 provides that a company is presumed to be unable to pay its debts if the company has failed to comply with a statutory demand.

[25] On this, Brookers Company & Securities Law Volume 1 at para. CA241.03 provides in part:

> "Section 288(4) expressly provides that in determining whether a company is unable to pay its debts, its contingent and prospective liabilities may be taken into account. The "cash flow" test of solvency, based on the ability of a company to pay its debts, must be contrasted with the "balance sheet" test of solvency which is concerned with whether the value of a company's assets exceeds the value of its liabilities. In determining whether the liquidation of a company can be justified under s 241(4)(a), it is the cash flow test that counts. This point was addressed by Plowman J (at p 410; p 40) in *Re Tweeds Garages Ltd* [1962] Ch 406; [1962] 2 WLR 38:
>
> > "In such [cases where a company is unable to meet the current demands on it it is useless to say that if its assets are realised there will be ample to pay 20s in the pound: this is not the test. A company may be at the same time insolvent and wealthy. It may have wealth locked up in investments not presently realisable; but although this be so, yet if it have not assets available to meet its current liabilities it is commercially insolvent and may be wound up."
>
> This passage was quoted by Associate Judge Doogue in *Commissioner of Inland Revenue v F B Duvall Ltd* (2009) 24 NZTC 23,135, at para 10. In that case the Court held that the need to establish solvency cannot be discharged by showing that the defendant can pay one of its creditors. Once the presumption of insolvency was established (such as failure by the defendant company to comply with a statutory demand) it would be necessary to show that the company was solvent. Solvency can only be demonstrated if it is shown that the company can pay its debts generally. The defendant in this case had made a bold statement that it was able to pay its debts and had exhibited its financial statements to a sworn affidavit, showing shareholders funds of $5 million or more. This was not enough. (For example, shareholders funds may include debts owed by other persons that are not likely to be recovered.) The defendant should have also adduced evidence that the company's financial statements provided a fair and accurate view of the company's financial position."

[26] In considering s. 241 Companies Act 1993, Brookers Company & Securities Law Volume 1 at para. CA241.04 notes the limited discretion the Court retains to refuse an order for liquidation under certain circumstances. The learned authors state:

> "**CA241.04 Appointment of the Liquidator – at Court's Discretion**
>
> Even if the applicant has standing to institute the liquidation process before the Court and it is found that the facts support one or other of the grounds for the appointment of the liquidator, the Court reserves the right to refuse to put a company into liquidation. The Court will exercise this jurisdiction sparingly. The normal rule is that if the relevant requirements have been met, the person making the application is entitled to his or her order for the company's liquidation. This is so even if it is shown that in the liquidation it is unlikely there will be any assets available for distribution to the unsecured creditors. In cases such as this, often the Court still regards the liquidator as serving useful functions in the investigation of the company's affairs and is acting as a guardian of the interests of the unsecured creditors….".

[27] In the present case the first ground of defence argued for the defendant is that the amount claimed in the plaintiff's statutory demand has been satisfied. As I have

noted at para. [11] above that statutory demand claimed the sum of $809,359.99 and required payment by the end of November 2008. In fact, the final amount due under the statutory demand was not cleared until 21 August 2009 when the present liquidation application was about to be heard.

[28] Counsel for the defendant raises the issue as to whether upon full payment of this statutory demand debt the plaintiff continued to have standing to apply to put the defendant company into liquidation. In this regard, counsel refer to comments made by Master Thompson in *Airborne Freight Limited v Fastway Express Parcels (NZ) Limited* (1994) 7 PRNZ 372 and in McGechan on Procedure at para. HR31.11.04. The comment in McGechan at para. HR31.11.04 notes:

> "In a case where the full amount has been paid over as security, it is difficult to imagine a situation where a liquidation order would be justified …. This approach was approved by Master Thompson in *Airborne Freight Limited v Fastway Express Parcels (NZ) Limited* ….".

[29] This passage in McGechan and the decision in *Airborne Freight Limited* were considered recently by Associate Judge Osborne in *Commissioner of Inland Revenue v The Fish & Chip Shop Company Limited* High Court, Christchurch, 21 July 2009, CIV-2009-409-672 where at para. 53 he states:

> "53. As a general proposition the McGechan passage uncomplicated by the context of an increasing debt is a passage I would accept and adopt in its context. But when applied to a defendant whose debt is increasing as a result of a statutory regime week by week and against a background of presumed insolvency or evidence of insolvency, I do not consider *Airborne Freight* particularly assists in this context."

[30] This particular question was also addressed in a decision of Associate Judge Doogue in *Magic Carpet Rides Limited v ACS 2006 Limited* High Court, Auckland, 5 August 2009, CIV-2009-404-2130. Addressing these issues Associate Judge Doogue stated at paras. [18] and [19]:

> "[18] I do not accept Mr Thwaite's (counsel for the defendant) submissions. The statutory demand that was served gave rise to a rebuttable presumption of insolvency. The presumption of insolvency arose because the debt, which was the subject of the statutory demand, was not satisfied within the time limited for doing so, namely 10 working days. Nor was the statutory demand set aside. It therefore took effect and gave rise to the presumption that I have just mentioned. It would not matter if that debt were subsequently repaid. The significance of the statutory demand is that the debt was not paid punctually as required by the statutory demand

> and that failure to pay within the time limited by sections 289 of the Companies Act 1993 is what gives rise to the presumption of insolvency.
>
> [19] Once the presumption of insolvency arises, a liquidation proceeding has to be commenced within 30 working days after the last date for compliance with the demand. But the result is that the plaintiff may start proceedings based upon the insolvency of the company and pray in aid the presumption of insolvency even although the particular amount which was the subject of the statutory demand had since been repaid. But the plaintiff, when it commences proceedings to liquidate the company, must do so as a 'creditor' of the company. There must be an extant debt. That debt can have arisen since the statutory demand was served and indeed arise out of different circumstances."

[31] In the present case, although the debt in the statutory demand was finally settled by the defendant at the eleventh hour on 21 August 2009, substantial additional taxes, interest and penalty had accrued. As I have noted at para. [17] above, the amount certified by the plaintiff as outstanding from the defendant as at 1 October 2009 was $1,308,325.77. The plaintiff therefore clearly retains the position of a "creditor" of the defendant. This debt to the plaintiff, which has not in any way been disputed by the defendant, is one which has increased week by week as a result of the statutory regime for payment of various taxes by the defendant.

[32] I accept and adopt here the approaches of Associate Judge Osborne in *Commissioner of Inland Revenue v The Fish & Chip Shop Co Limited* and of Associate Judge Doogue in *Magic Carpet Rides Limited v ASC 2006 Limited*. The passage in McGechan referred to at para. [28] above and the decision in *Airborne Freight Limited* in my view relate to the situation where all debt has been paid over or secured to the creditor and no monies are outstanding between the parties. This is not the situation here. For all these reasons I reject the defence which the defendant has endeavoured to advance that the statutory demand has been satisfied and therefore the plaintiff has no standing to bring this application.

[33] The second ground of defence advanced by the defendant here suggested that the residual discretion the Court retains as to whether or not to make a liquidation order, noted at para. [26] above, ought to be exercised against the making of the order for several reasons. I will deal with each of these reasons in turn:

A. Length of Time Since Statutory Demand Served

[34] The statutory demand as I have noted was served on 6 November 2008 and the defendant company is presumed to be insolvent when it failed to pay the amount demanded by 27 November 2008. Counsel for the defendant contends that since that time the company made determined efforts to resolve its difficulties. Finally, on 21 August 2009 the balance owing under the statutory demand was paid. Counsel suggests that the length of time that has elapsed since service of the statutory demand must count against the exercise of the discretion in favour of the plaintiff here.

[35] I reject this contention. No explanation is given by counsel for the defendant as to why any delay should favour the defendant in the exercise of the Court's discretion. Despite numerous calls of this matter that delay occurred essentially to allow the defendant every opportunity to clear all outstanding debt to the plaintiff which it has not done. There is no substance in this ground of defence advanced for the defendant.

B. Change of Position by Plaintiff

[36] The next ground advanced for the defendant concerning the exercise of the Court's residual discretion relates to the defendant's claim that it understood up to the call of this matter on 20 August 2009 the plaintiff was prepared to withdraw the present liquidation application if the $809,359.99 debt referred to in the statutory demand and statement of claim was settled. This contention, however, is strongly disputed by the plaintiff. In any event it is rejected because even if there may have been some understanding regarding withdrawal of the liquidation application upon payment by 20 August 2009 of the statutory demand amount, this did not occur. It was not until the further adjourned call on 21 August 2009 that the balance $253,851.01 of this debt was paid and in the mean time substantial other tax debt had accrued. This further ground of defence advanced for the defendant is also rejected.

C. Solvency - Net Assets and Current Trading Position of the Defendant

[37] The next ground of defence for the defendant, as I understand it, is that the company is effectively solvent. On this, I accept that the fact of solvency if established, is usually relevant to the exercise of the Court's discretion, essentially to prevent abuse of process. The defendant's initial contention was that the net assets of the company as shown in its annual report as at 31 March 2008 were substantial. In his 21 August 2009 affidavit, Mr. Thurston deposed:

> "ACL is trading profitably. When selling its Hastings properties it will be taking a lease back to enable it to continue its business at that site. The proceeds of sale will totally repay the ANZ Bank and leave a significant unsecured surplus available to ACL."

[38] Subsequent to this 21 August 2009 affidavit, Mr. Thurston has sworn a second affidavit on 18 September 2009. This affidavit includes as an annexure a 1 page "Statement of Financial Position as at 18 September 2009" for the company.

[39] This Statement of Financial Position it seems was prepared by Mr. Thurston or employees of the defendant at his direction. It was not prepared by independent accountants nor has it been verified by any independent party. This is despite the specific request at para. [32] of my judgment of 27 August 2009 in granting the adjournment then sought by the defendant that this adjournment was:

> "…. To allow the defendant an opportunity to provide the Court with detailed and independent verification of its solvency both on the basis of its asset and liability position and the "cash flow" test …".
>
> (emphasis added)

Despite this plea, the defendant has chosen to simply place before the Court its own unverified statement of financial position and certain other financial information and projections.

[40] Turning for a moment to that 18 September 2009 Statement of Financial Position, it purports to show total assets of $44,835,937.00, total liabilities of $22,955,507.00 and equity of $21,880,430.00. Included in the current assets listed for the defendant are $11,167,872.00 as "related party loans". These related party loans are not in any way itemised. Strong issue is taken with this by Mr. Light in his

24 September 2009 affidavit for the plaintiff. At para. 11 of this affidavit, Mr. Light notes that the plaintiff has already served statutory demands on four companies closely related to the defendant (who have been the beneficiaries of substantial related party loans) being Tawera Land Company Limited, Sheddan Investments Limited, Advanced Logistics Limited and Aotearoa Resorts Limited. He contends this must shed considerable doubt upon the total in this related party loans entry, given that in the defendant's 30 June 2008 Financial Statements annexed to Mr. Thurston's first affidavit, the related party loans to these companies alone were shown at a figure of nearly $8 million.

[41] Further, in the 18 September 2009 Statement of Financial Position for the defendant property, plant and equipment is noted at $31,650,065.00. Again, there is an absence of comprehensive up-to-date valuations or any effective verification for this substantial property asset claim before the Court.

[42] Given the length of time that has elapsed since the 18 December 2008 commencement of these liquidation proceedings and noting the comments made at para. [32] of my 27 August 2009 judgment, it is unfortunate that the defendant has been unable to place before the Court independent verification of these important figures.

[43] And, in addition, the claim advanced before me by counsel for the defendant that it has brought its current obligations to the plaintiff from its trading activities up to date must be under considerable question. From the Certificate of Indebtedness placed before the Court by the plaintiff it is clear that in addition to substantial arrears, current GST payments as assessed by the defendant itself which were due for the month ending 31 July 2009 (payable in August 2009) totalling $71,315.01 and for the month ending 31 August 2009 (payable in September 2009) totalling $110,394.57 remain unpaid. Given the position in which the defendant company found itself with this liquidation hearing scheduled for 1 October 2009, and its claim to have substantial assets, it is significant that these current GST tax liabilities were not paid and remain overdue.

[44] Although it is clear from the authorities that the Courts have been prepared on occasions to restrain liquidation proceedings if a debtor company is able to establish that it was in fact solvent, as McGechan on Procedure at para. HR31.11.04 notes:

> "In most cases, a claim of solvency would be accompanied by some sort of dispute as to the amount claimed by the creditor."

[45] In the present case there is no dispute as to the debt of over $1.3 million which the plaintiff certifies is currently outstanding from the defendant. Further, the onus is clearly on the defendant to establish by properly verified information that it is solvent. The material which has been provided to the Court in this case is not verified by any independent source.

[46] Nevertheless, even if I were to accept for a moment that the defendant company's assets exceed its liabilities as it claims, this would only satisfy one element of the required solvency test. The second element of this test is that the defendant must show an ability to meet its financial obligations as they become due. As I have noted at para. [25] above this "cash flow" test of solvency is critical in determining whether liquidation of a company can be justified under s. 241(4)(a) Companies Act 1993.

[47] As Master Venning as he then was noted in *Investment Enterprises Limited v Private Sale Company Limited* (1997) 10 PRNZ 282 at 285:

> "The onus is clearly on the defendant company to prove its ability to pay its debts and to rebut the statutory presumption. I accept Mr Forbes' submission that the appropriate test is as set out in *Re Tweeds Garage Limited* (1962) Ch406. The test is whether the company is able to meet current demands on it, including assets currently realisable."

[48] In the present case Mr. Thurston for the defendant contends that a number of its creditors have agreed to a time payment arrangement. There is nothing in the evidence provided for the defendant, however, to address the substantial amount still outstanding to the plaintiff which includes the last 2 months' GST debts.

[49] The only evidence as to solvency advanced on behalf of the defendant company here is provided in the affidavits of Mr. Thurston. Principally this

addresses what he says is the asset and liability position of the defendant. The defendant's ability to meet current demands made upon it including the ease with which assets it holds could be realised to clear debts is entirely uncertain.

[50] Mr. Thurston's 18 September 2009 second affidavit does purport to annex details of what he says are "Receivables as at 21 September 2009" and profit and loss statements for May, June, July and August 2009. Prospective financial information for the year ending 31 August 2010 is also exhibited. None of this material is in any way independently verified however nor is it clear from these accounts whether the company, in the short term will be able to meet its current debts and the demands made upon it.

[51] There is no doubt in my mind that the defendant has not satisfied the onus upon it to prove its ability to pay its debts in terms of meeting current demands on it and thus satisfying the established "cash flow" test. What material the defendant has placed before the Court is confusing and in many areas sketchy at best. In my view, given particularly that there is no independent verification of this information, must mean that it is quite inadequate to satisfy the Court that the defendant has proved it is solvent to the required standard.

Conclusion

[52] I conclude that the defendant company is insolvent in the sense that it is unable to pay its debts and there is no discretionary reason why an order for the appointment of liquidators should not be made here.

[53] Despite this conclusion, however, it needs to be noted that before me, Mr. Ryan for the defendant contended that in the event I did reach this position, the defendant company should be provided with one last opportunity to settle the $1,308,325.77 debt certified as due to the plaintiff before the Court proceeds to the serious step of making an order for the appointment of liquidators. This submission was based in part upon matters referred to by Mr. Thurston in his 1 October 2009 third affidavit filed in this proceeding. Annexed to this affidavit as Exhibit "E" is an email from South Canterbury Finance Limited which purports to provide a

conditional offer of finance to the defendant to settle the debts owing to the plaintiff and other creditors. There is clearly some way to go, however, before this conditional finance offer can mature into a permanent loan advance to clear the defendant's current debts. But Mr. Ryan for the defendant urged upon me the argument that the defendant should be afforded this opportunity.

[54] On this, I note that in *Commissioner of Inland Revenue v Ron West Motors (Otahuhu) Limited* [2008] 23 NZTC 21, 835 and in *Commissioner of Inland Revenue v FB Devale Limited* where the Courts were faced with a similar issue, in each case short adjournments were provided to give the defendants an opportunity to clear the debts in question.

[55] In the present case the defendant company has had what I see as many opportunities to clear its ongoing debts to the plaintiff. Notwithstanding that, in my view, it is appropriate in the circumstances of this case that the defendant should be given one final opportunity to clear its debts which it contends that it can do. I say this bearing in mind the defendant's evidence that it is continuing to trade profitably.

[56] I therefore adjourn this proceeding to a call in my next liquidation list in the Palmerston North High Court on 5 November 2009 at 10.45 am for further mention. If the defendant has been unable to make arrangements to clear these outstanding current debts in a proper manner by that time then an order for liquidation is likely to follow.

[57] In the mean time costs are reserved.

'Associate Judge D.I. Gendall'