IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV 2008-404-004443

UNDER	THE COMPANIES ACT 1993
BETWEEN	BASTIN ENTERPRISES LIMITED Applicant
AND	GRANT RONALD GRAHAM AND BRENDON JAMES GIBSON Respondents

Hearing: 12 December 2008

Counsel: J A MacGillvray and M S Crockett for applicant
L A O'Gorman and N K King for respondents

Judgment: 4 November 2009 at 3:00pm

JUDGMENT OF ASSOCIATE JUDGE ABBOTT

This judgment was delivered by me on 4 November 2009 at 3:00pm, pursuant to Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Solicitors:
Tompkins Wake, PO Box 258, Hamilton 3240 for applicant
Buddle Findlay, PO Box 1433, Auckland 1010 for respondents

[1] Bastin Enterprises Limited (Bastin) has applied for leave to bring a claim against Jabroni Investments Limited (in liquidation) (Jabroni). The application is opposed by the liquidators (G R Graham and B J Gibson).

[2] Jabroni was formally called Beds R Us 2003 Limited. It was the franchisor of the Beds R Us franchise (in the business of retailing of beds). Bastin operates furniture retailing stores. It entered into four franchise agreements with Jabroni which included provision for Jabroni to indemnify Bastin for losses suffered in the franchise business if certain conditions were met.

[3] Bastin's four Beds R Us franchises were unsuccessful. It made claims on Jabroni under the indemnities. There was a dispute as to whether the terms of the indemnity were met and Jabroni declined to pay. Bastin prepared a Court proceeding against Jabroni to enforce its claim. Before that proceeding was filed Jabroni's shareholders placed it into voluntary liquidation, after assigning its rights under the franchise agreements to a company that had taken over the premises and the franchise businesses that Bastin had been operating, leaving only liabilities in Jabroni.

[4] Bastin filed a proof of debt for the sum sought under the indemnity. The liquidators rejected it on the grounds that the claim could not succeed as Bastin had not met the terms for indemnity under the franchise agreements. They oppose leave being granted for the same reason, and also because it is not appropriate for Bastin, in effect, to be given a second opportunity to pursue the same claim.

[5] Counsel were agreed that the essential issue is whether it is appropriate to grant leave to issue a new proceeding in circumstances where Bastin had already sought and been given a determination of its claim by the liquidator.

Background

[6] Jabroni was incorporated in October 2003 by brothers Craig Turner and Graeme Turner. The brothers were the principal parties behind bed manufacturing company Sleepyhead Manufacturing Company Limited (Sleepyhead). Sleepyhead and a number of bedding retailers formed a trading group known as the Beds R Us group using the Beds R Us brand. Subsequently the Turners established Jabroni as franchisor of a franchise business using the Beds R Us brand, with bedding retailers in the Beds R Us group forming the core of the franchisees.

[7] Bastin was a bedding retailer with a long standing contractual relationship with Sleepyhead. It was one of the retailers in the Beds R Us group. Initially Bastin resisted the franchise proposal promoted by the Turner brothers (there was an issue as to whether the Beds R Us group or Sleepyhead was entitled to the Beds R Us brand). It had concerns about profitability because the franchise arrangements would not permit Bastin to combine an existing general furniture franchise business in its four Auckland stores with the franchised bedding business. Bastin eventually accepted the franchise proposal after it was agreed that the agreements for the four Auckland stores would include what was referred to as a "loss underwrite" clause. Bastin was the only franchisee with this special clause in its franchise agreements.

[8] Bastin entered into the four franchise agreements (one for each of its Auckland stores) with Jabroni on 14 October 2003. Under the loss underwrite clause Jabroni agreed to indemnify Bastin for any loss incurred in the operation of the franchise business, on certain terms set out in detail in sub clause 24.3 of the agreement. These terms included the provision of specified financial information within defined periods. The terms also included an entitlement for Jabroni to give directions to Bastin as to management and operation of the franchise businesses, including a direction to cease trading (with any losses incurred as a result also being subject to the indemnity).

[9] Bastin's director and principal shareholder, Mr Graeme Bastin, met monthly with Mr Craig Turner (who I will refer to in future as Mr Turner) from November 2003 onwards to review the financial performance of Bastin's four franchises. It is

common ground that Mr Bastin provided financial information about the stores at these meetings, but there is a dispute as to the precise information provided. Although this is strongly in dispute, Bastin contends that there was an agreement that the information provided was sufficient to satisfy the requirements of clause 24.3.

[10] Bastin suffered trading losses from the outset of the franchise businesses. In May 2004 Bastin submitted an invoice, pursuant to the loss underwrite clause, for losses to 31 March 2004. Jabroni paid that invoice in September 2004. In June 2005 Bastin submitted a second invoice, this time for losses to 31 March 2005.

[11] In early 2005 Jabroni advised Bastin that it was exercising its right to direct Bastin to dispose of the loss making businesses. On 1 July 2005 Bastin sold the four Auckland stores to Menton Operations Limited (a company in which the Turners were beneficially interested). Following that sale Bastin sought payment of its second invoice, and submitted two further invoices for its losses.

[12] On 22 December 2005, Jabroni changed its name from Beds R Us 2003 Limited and was placed into voluntary liquidation. At an unknown date prior to that, all of its franchise agreements had been transferred to a further company associated with the Turner brothers' interests.

[13] On 14 February 2006 solicitors acting for the Turner interests wrote to Bastin's legal adviser rejecting its outstanding claims under the loss underwrite clause on the ground that Bastin had failed to comply with its obligations to provide the financial information specified in the clause.

[14] On 27 February 2006 Bastin lodged an unsecured creditor's claim with Jabroni's liquidators for the total amount of its three outstanding invoices ($851,218). Over ensuring months the liquidators considered the claim and sought further information from Bastin. Bastin's solicitors provided the liquidators with a substantial package of information on 19 December 2006. After reviewing that information the liquidators met with Mr Bastin on 31 May 2007 and they sought further information on matters arising out of that interview.

[15] On 7 September 2007 the liquidators wrote to the solicitors for the Turner interests advising that they intended to admit Bastin's claim in respect of trading losses to 31 March 2005 ($435,877) unless they had any information to the contrary. The solicitors for the Turner interests responded on 20 September 2007 contending that Bastin's claim should be rejected in its entirety on two grounds. The first was the failure to comply with obligations to provide financial information. The second was that the right to claim fell away after assignment of the franchise agreements.

[16] By this time the issue over compliance with clause 24.3 had become prominent. Bastin had told the liquidators that it had been agreed in the monthly meetings with Mr Turner that the information which Mr Bastin was providing for those meetings was sufficient, notwithstanding the specific terms of the clause. The liquidators sought comment from the Turner interests on the possibility of variation or waiver of the loss underwrite clause. They indicated that on the basis of the information received from Mr Bastin it appeared that the parties had agreed terms other than those set out in the clause, and had conducted themselves accordingly.

[17] The solicitors for the Turner interests responded by pointing to non waiver clauses in the agreements, and providing a formal written statement by Mr Turner that he had made no statements nor otherwise given Mr Bastin any reason to believe that the financial obligations had been waived or were varied.

[18] Faced with this conflict, the liquidators informed the solicitors for the Turner interests that they would require an indemnity from them for any costs that they may incur as a result of Bastin challenging a rejection of its claim. The liquidators advised Bastin's solicitors in December 2007 that they had received the statement from Mr Turner. Their response, in early January 2008, was that the contentions were not credible, and that the liquidators had to make their decision.

[19] On 30 April 2008 Bastin served the liquidators with a notice under the Companies Act 1993 requiring a determination of its claim, failing which Bastin would apply to the High Court for an order to that effect. The liquidators did not respond within the period stated in the notice, and Bastin filed an application on 9 May 2008.

[20] On 18 June 2008 the liquidators received a deed of indemnity signed by the Turners. They issued a notice of their decision to reject Bastin's claim on 20 June 2008.

The application

[21] In its application Bastin applied for leave to apply under s 284 of the Companies Act 1993 to seek reversal of the liquidators' decision to reject its proof of debt (and for that order) and, alternatively, for leave under s 248 of the Companies Act 1993 to bring a proceeding against Jabroni in which to establish its claim. At the hearing Bastin limited its application to seeking leave to commence its proceeding against Jabroni under s 248, as the more appropriate course given that the liquidators' evidence in opposition to the application raises direct conflicts of fact.

Applicable principles

[22] Bastin seeks leave under s 248(1)(c) of the Companies Act 1993. It is common ground between counsel that the Court has a wide discretion. As with any discretion, however, it must be exercised on a principled basis. Factors which the Court will take into account in the exercise of its discretion were helpfully summarised in *Fisher v Isbey* (1999) 13 PRNZ 182 (at para [19]). Those factors and others identified in *Birchall v Project Works Construction Limited (in liquidation)* (2004) 9 NZCLC 263, 547 have recently been applied in this Court in *I H Wedding & Sons Limited & Anor v Buy-Sell Realty NZ Limited* (HC AK CIV 2008-404-005502, 27 November 2008, Allan J). I adopt the following summary from the latter case at para [12]:

> a) The requirement for equality among creditors;
>
> b) The consideration that the assets of the company should not be dissipated in wasteful litigation, particularly if there is a more convenient method of determining the claim;
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> c) The need for consideration of the alternative procedure prescribed by s 302 of the Act, coupled with the Court's power of review in s 284(1)(b);

d) The proposed claim must be shown to be not unsustainable, but beyond that the Court should not examine the merits of the case;

e) Where the relevant proceedings, even if successful, are likely to be fruitless, leave will often be declined;

f) Delay by an applicant may justify the refusal of leave;

g) Overall, the onus is on the party seeking leave to satisfy the Court that leave should be given.

The competing arguments

(a) *Bastin's arguments*

[23] Counsel for Bastin submitted that the Court should have regard to the context of this dispute in exercising its discretion. He argued that this was not an ordinary liquidation for the failure of a trading company. He said that Bastin wished to establish its status as a creditor to give it standing to pursue claims against the Turners and Sleepyhead in respect of what has turned out to be a worthless indemnity in the franchise agreement. Counsel submitted that it was more appropriate to resolve Bastin's claim (and hence its status as a creditor) in a specific proceeding for that purpose, rather than by challenge to the reasonableness of the liquidators' determination, because an ordinary proceeding with discovery and examination in that was more appropriate than a summary application to resolve issues of disputed fact that were central to the determination.

[24] Although counsel contended that one of the important issues of fact related to the financial information that was in fact supplied to Jabroni, he placed greater weight on Bastin's argument that Jabroni (through Mr Turner) had waived the requirement of clause 24.3, or by reason of his conduct in accepting information without demur, was estopped from insisting on strict compliance with the obligation to provide financial information in specific form. Counsel argued that this issue in particular could not be addressed satisfactorily in the summary process of reviewing the liquidators' decision pursuant to s 284 of the Companies Act 1993. He also submitted that there were no creditors other than the Turner interests who were likely to be affected, and that the claim would not be futile given Bastin's intent to pursue

claims against the Turners (as de facto directors of Jabroni) and against Sleepyhead (under the pooling provisions of the Companies Act 1993).

(b) The liquidators' arguments

[25] Counsel for the liquidators focused her argument on the contention that Bastin had already sought and obtained a determination of its claim by the liquidators. Although she accepted that it would have been open to Bastin to have sought leave to commence a proceeding at the outset, it had chosen instead to pursue its claim in the liquidation (with knowledge of the opposition to its argument on waiver and estoppel). She argued that, in the interests of finality and certainty, Bastin should not be permitted to re-litigate the same claim again in a separate proceeding if it could not show that the liquidators' decision was unreasonable. She referred to the extensive and cautious approach that the liquidators had taken in their investigation of the claim, and submitted it was reasonable for the liquidators to have rejected the claim both for failure to comply with the terms of the loss underwrite clause and to dismiss the claim for waiver or estoppel on the information provided to them. She submitted that it was not necessary to determine the disputes of facts as the allegation of waiver or estoppel could not be established even on Mr Bastin's evidence.

Factors bearing on discretion

[26] The following factors emerge from the opposing arguments as requiring consideration by the Court:

a) Whether the claim that Bastin wishes to bring is "not unsustainable".

b) Whether there are reasons to allow Bastin to pursue the claim in a separate proceeding, given that the liquidators have already considered and determined it.

c) Whether there is any issue as to equality among creditors, unnecessary dissipation of assets or futility of the proposed claim.

d) Overall, whether Bastin has met the onus of satisfying the Court that leave should be given.

Does Bastin have a sustainable claim?

[27] The currently accepted approach (set out in *Fisher v Isbey*, and endorsed in *I H Wedding & Sons Limited v Buy-Sell Realty NZ Limited*) is that leave should be declined for a proceeding which is "clearly not sustainable", but otherwise the Court will not enquire into the merits of the proposed claim. Associate Judge Lang (as he then was) commented on this threshold in *Trinity Foundation (Services No 1) Limited v Downey* (2005) 9 NZCLC 263,917, when considering an application for leave to bring an application under s 284 of the Companies Act 1993 (reversing or modifying a decision of liquidators):

> [16] In *Fisher v Isbey* (supra) Master Faire held (at para [23]) that, although the Court should decline to grant leave to a creditor to bring proceedings that are clearly not sustainable, it would generally not enquire into the merits of the proposed claim.
>
> [17] In considering the threshold postulated by Master Faire, I accept that the Court would generally decline an application for leave to commence or continue proceedings under s 248 in circumstances where, for example, the proposed claim was clearly statute barred by virtue of the provisions of the Limitation Act 1950 or where it would not survive a strike out application. In the absence of circumstances of that type, however, the merits of the claim should not generally be the subject of consideration in an application for leave under s 248. Instead, the focus will generally be upon the most convenient and cost effective way in which the creditor's claim can be established.

[28] Although Bastin says that it is currently unclear exactly what information was provided to Jabroni in the monthly meetings between Mr Bastin and Mr Turner, there seems little doubt that Bastin did not provide the formal accounts and forecast of profitability contemplated by clause 24.3(f) of the franchise agreements within the prescribed time period, if at all. Bastin acknowledges that it has a computerised accounting system, yet Mr Bastin produced only handwritten extracts from the computer records, and other summaries of information. He says that Mr Turner accepted this information as providing all that was necessary. That is where the real contest lies. Bastin argues that this was sufficient to constitute a waiver by Jabroni, or alternatively that Mr Turner's failure to raise issues about that information (until

its solicitor's letter in January 2006), and acceptance of Bastin's first claim without requiring strict compliance with clause 24.3(f), gave rise to an estoppel.

[29] Counsel for the liquidators submitted that the evidence of Mr Bastin did not establish either "the distinct, intentional and knowing act required to constitute waiver" (*Land & National Development Corporation Pty Limited v Tatebrook Pty Limited* [1999] NSWSC 669 at para 40) or the unequivocal promise or legal representation required to give rise an estoppel.

[30] She further submitted that the argument on waiver was unsustainable in light of clause 20.5 of the franchise agreements:

> 20.5 No failure by the Franchisor to take action on account of any default by the Franchisee whether in a single instance or repeatedly will constitute a waiver of any such default or of the performance required of the Franchisee. No express waiver by the Franchisor of any provision or performance of an obligation of the Franchisee under this Agreement or of any default the Franchisee will be [sic] constitute a waiver of any other or future provision, performance or default.

[31] In response to the latter submission counsel for Bastin argued that the clause should be construed restrictively (contra proferentem) and was limited to matters where Jabroni could be expected to "take action on account of any default". He submitted that it was open to the parties to have excluded all waiver (by clear and direct language), but the clause did not go that far. He said that *Land & National Development Corporation Pty Limited v Tatebrook Pty Limited* did not apply as the clause in that case required all waivers to be in writing.

[32] I am not persuaded that Bastin's claim to waiver is clearly not sustainable. Leaving aside the exclusion clause, on Mr Bastin's evidence Mr Turner appears to have been prepared to disregard the obligations under clause 24.3. This would appear to bring the case within the terms of the following passage from *Craine v Colonial Mutual Fire Insurance Co Limited* (1920) 28 CLR 305, 326 (cited in paragraph 40 of *Land & National Development Corporation Pty Limited v Tatebrook Pty Limited*

> A waiver must be an intentional act with knowledge. First, some distinct act ought to be done to constitute a waiver, next it must be intentional, that is, such as either expressly or by imputation of law indicates an intention to treat the matter as if it did not exist or as if the forfeiture or breach of condition had not occurred; and lastly it must be with knowledge.

[33] Bastin's case in respect of the exclusion clause (20.5) is less strong. Even if it is construed contra proferentem, it is difficult to see how a failure to take issue with the form of the accounts, in the absence of any statement that the information provided was sufficient, could be other than a failure to take action in respect of performance required of Bastin.

[34] Counsel for Bastin acknowledged the possibility that clause 20.5 could present Bastin's claim to waiver, but argued that it would not oust the doctrine of equitable estoppel. He relied on the summary of the elements of that doctrine in *Goldstar Insurance Co v Grant* [1998] 3 NZLR 80, 86. He submitted that Mr Turner's agreement to attend monthly meetings, and acceptance of the information supplied by Mr Bastin without requiring more, together with Jabroni's payment of Bastin's first claim, created a reasonable expectation or belief that the information provided discharged its obligations under clause 24.3. He said that Bastin's case would be that there was an agreement to this effect, but in any event that it would be unconscionable to allow any departure from that expectation.

[35] If an agreement to accept the information provided by Mr Bastin is established, that would seem to constitute either a variation to or waiver of clause 24.3. It might also fall within the limited circumstances where silence or an omission to act could amount to a representation giving rise to an estoppel (*Goldstar Insurance Co v Grant* at p 87).

[36] Counsel for the liquidators argued strongly that the evidence before the Court did not provide any support for the alleged agreement. She submitted that Mr Bastin appeared to have expanded an initial allegation of silence or inaction into an agreement (in his affidavit in support of this application), but failed to provide any deeper matters supporting such agreement other than Mr Turner's silence when presented with the financial information. She also submitted that an estoppel could

not arise in the absence of a legal duty to act: Spencer Bower and Turner, *Estoppel by Representation* (3rd ed; 1997) para 55.

[37] There is some strength to the points made by counsel for the liquidators as to the apparent inconsistency between Bastin's initial position (a complaint as to silence on the part of Mr Turner) and its present position (an agreement that the information was sufficient). However, all that Bastin needs to establish at this stage is that its claim is not clearly unsustainable. Although Bastin appears to face a number of difficulties with its claim, I am not persuaded that it is clearly not sustainable as would be the case, for example, if the claim was time-barred.

Are there reasons for allowing a further and separate claim?

[38] There is substantial merit to the liquidators' case that Bastin's claim was capable of being dealt with in the liquidation. That is the natural inference to be taken from Bastin's submission of a proof of debt, and its insistence that the liquidators make a decision on that claim even after the arguments now before the Court had emerged. Counsel for Bastin raised three matters which he submitted needed to be determined in an ordinary proceeding with the benefits of discovery and full trial:

a) Whether the information provided by Bastin to Jabroni complied with clause 24.3;

b) If it did not, whether Jabroni was estopped from relying on its strict rights under clause 24.3 by reason of conduct leading Bastin to believe that the information it was providing was sufficient; and

c) Whether Bastin's failure to submit claims for losses after the forced sale of the Auckland stores within the prescribed period was due to Jabroni's failure to provide information in a timely fashion.

[39] I am not persuaded that a separate proceeding is required to determine the first and third of these matters. The liquidators held all Jabroni's documents, and

were provided with documents by Bastin. I consider that the liquidators were able to determine compliance based on documents provided by Bastin and their interview with Mr Bastin. Even if they did not use it (there is no evidence on this before the Court), the liquidators also had powers to seek any further information from Jabroni's directors or Mr Turner if they felt it was available and could assist. The same applies to Bastin's complaint that Jabroni failed to provide information sought by Bastin in respect of losses after the sale of the Auckland stores (the third and fourth invoices).

[40] The critical issue is that of the conduct of Mr Turner in the meetings to discuss the financial performance of Bastin's stores. As I have referred to earlier, counsel for the liquidators argued that this point could be determined on Mr Bastin's own evidence. I have already found that the claim is not unsustainable. Counsel endeavoured to persuade me that I should not allow Bastin a second opportunity to establish its claim where the liquidators' decision could not be shown to be unreasonable. I do not consider that I should limit the consideration in that way (it would be tantamount to accepting the wider test applicable to an application for leave under s 284 that the claim must be arguable and that the liquidators' decision must be capable of being set aside as unreasonable): *Trinity Foundation (Services) No 1 Limited v Downey* para [21]. The liquidators quite clearly had difficulty with this aspect of the claim. The fact that they did not make a determination until receiving an indemnity from the Turners indicates to me that they were unable to resolve the point with any certainty. It is an issue more suited to resolution in a Court proceeding than by liquidators in the course of administration, even when coupled with the Court's power of review under s 284(1)(b).

[41] I do not consider that Bastin's initial election to have its claim accepted in the liquidation is necessarily inconsistent with leave being given for a separate proceeding. I suspect that the application for leave to commence the separate proceeding was initially included in Bastin's application to meet any argument that the claim should not be dealt with under s 284(1). The decision to seek leave only for a separate proceeding was made after it became apparent that there was an unresolvable conflict of evidence in respect of the meetings between Mr Bastin and Mr Turner.

Other factors

[42] I am not persuaded that there are any other factors which necessarily count against granting leave. The liquidators have not contested Bastin's case that there are no other creditors (apart, perhaps, from Turner interests). Given the Turners' direct interest in the matter, I do not consider the requirement for equality among creditors to be significant. Similarly, as there are no assets left in Jabroni, it cannot be said that they will be dissipated in unnecessary litigation. Further, it cannot be said that it would be futile to give leave as the proceeding, if successful, would still be fruitless. It will have value for Bastin in establishing its status as a creditor, and thereby giving it the ability to pursue its intended claims against the Turners and Sleepyhead. I consider it appropriate, however, to echo the warning given by Master Faire in *Isbey v Fisher* that failure to succeed may well justify an order for solicitor/client costs in the substantive proceeding, particularly in light of what I consider to be a marginal case for leave.

[43] The last factor to address is the funding of any defence. I do not regard that as significant. The liquidators have received an indemnity from the Turners as the parties who would otherwise be interested in defending any claim. I imagine that they will fund any defence if they consider it to be in their interest to do so.

Overall

[44] Having weighed all of the above factors I have come to the view that this is an appropriate case for leave to bring a separate proceeding against Jabroni.

Decision

[45] I grant leave to Bastin to commence a legal proceeding against Jabroni Investments Limited (in liquidation) in order to allow Bastin Enterprises Limited the opportunity to establish its claim against the company in liquidation.

[46] In order to advance matters, I direct that any proceeding be issued within 20 working days (or such further time as the Court may allow on written application for extension).

[47] In the circumstances, I order that costs be reserved pending final determination of any claim that may be brought.

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Associate Judge Abbott