IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2008-404-6299

BETWEEN	FIFER RESIDENTIAL LIMITED Plaintiff
AND	LOWNDES ASSOCIATES Defendant

Hearing: 16 December 2009

Appearances: Mr C Walker for Plaintiff
Ms P Fee for Defendant

Judgment: 17 December 2009 at 4 p.m.

JUDGMENT OF ASSOCIATE JUDGE DOOGUE

This judgment was delivered by me on ***17.12.09 at 4 pm****, pursuant to Rule 11.5 of the High Court Rules.*

Registrar/Deputy Registrar

Date……………

Solicitors:
Gilbert Walker, P O Box 1595, Auckland
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Introduction

[1] The defendant has applied pursuant to Rule 5.45 of the High Court Rules for an order directing the plaintiff to give security for costs in respect of its claim against the defendant. The grounds stated in the application are that there is reason to believe that the plaintiff will be unable to pay the costs of the defendant if the plaintiff is unsuccessful and that it is in the interests of justice for an order for security to be meet.

[2] Rule 5.45 provides:

> **Order for security of costs**
>
> (1) Subclause (2) applies if a Judge is satisfied, on the application of a defendant,—
>
> …
>
> (b) that there is reason to believe that a plaintiff will be unable to pay the costs of the defendant if the plaintiff is unsuccessful in the plaintiff's proceeding.
>
> (2) A Judge may, if the Judge thinks it is just in all the circumstances, order the giving of security for costs.
>
> (3) An order under subclause (2)—
>
> (a) requires the plaintiff or plaintiffs against whom the order is made to give security for costs as directed for a sum that the Judge considers sufficient—
>
> (i) by paying that sum into court; or
>
> (ii) by giving, to the satisfaction of the Judge or the Registrar, security for that sum; and
>
> (b) may stay the proceeding until the sum is paid or the security given.
>
> ……

[3] I also intend to be guided by the following statement of principle taken from *Nikau Holdings Limited v Bank of New Zealand* (1992) 5 PRNZ 430, at 436 – 439. That statement of principle can be broadly summarised as follows:

> (1) The Court must first be satisfied that there is reason to believe that the plaintiff will be unable to pay the costs of the defendant if the plaintiff is unsuccessful;

(2) If the threshold test is met, the ordering of security for costs is discretionary with no predisposition one way or the other. The exercise of the Court's discretion should aim to balance the interests of the plaintiff and the defendant;

(3) As far as possible the Court should endeavour to assess the merits of the claim. A consideration of all the circumstances of the case is required.

Ability of plaintiff to meet defendant's costs

[4] If the plaintiff fails in its proceeding, party and party costs that are likely to be ordered will be substantial. At the present time the trial is expected to take some 10 days. Both parties offered their views on what level of costs would be awarded against the plaintiff under schedule 2B (see, generally, Part 14 of the High Court Rules), were it to be unsuccessful. Their estimates diverged considerably, with the defendant suggesting a figure of $112,640, but with Mr Walker, at the other end of the spectrum, suggesting that $36,800 would be ordered. I consider that the correct figure will be somewhere between the two and I will adopt for the purposes of this judgment the assumption that a figure of approximately $75,000 would be awarded. The issue then becomes whether, on the basis of the evidence, I am satisfied that the plaintiff will be unable to pay all or some of the costs that are likely to be ordered.

[5] This focuses attention on the financial position of the plaintiff. In approaching my task, I have not been assisted by the fact that financial statements for the plaintiff have not been provided. I accept that there is no onus on the plaintiff to do so. However, the plaintiff has detailed their position in statements made by shareholders of the plaintiff about the company's financial position. The absence of any financial statements as corroboration of these witnesses' accounts means that the figures that the witnesses offer might not be accepted as unconditionally giving an accurate picture of the plaintiff's financial position.

[6] The plaintiff says that the sole asset owned by the plaintiff is an advance (**"the advance"**) of $1,585,850.86 that it made to a partnership comprising two companies, St Stephens Investments Limited ("**St Stephens")** and Parnell Property Investments Limited (**"Parnell"**). Both of these entities are associated with Mrs Alexander, the wife of Mr Paul Alexander, a former director of the plaintiff but now

a bankrupt. Mr Alexander himself gave an affidavit in the proceedings in which he confirmed that the advance remains extant. The plaintiff also accepts that the loan is unsecured. I will say something additional about that advance further on in my judgment. The plaintiff's deponents say that the plaintiff company has no debts. Although the BNZ Bank has registered a financing statement against the plaintiff, supporting a security interest in all the company's present and after-acquired property, the plaintiff says that the company is not currently indebted to the BNZ.

[7] Much of the discussion at the hearing was concerned with the advance. Mrs Fee pointed out that there are some unusual features of the loan which raise questions about its recoverability. The first is that the loan is payable on demand, with the right to call up the loan on demand accruing after 1 April 2007. The loan agreement further provided (at clause 15) that if demand for repayment of the principal sum had not been made by 1 May 2007 then the <u>borrower</u> could at any time thereafter issue fully paid shares in the borrower to the value of the principal sum and the lender will accept such shares in satisfaction of the debt. The agreement also contained machinery for arbitrating any differences as to "whether such shares represent the value of the principal sum". The accountants appointed as part of that machinery are to specify the number of shares that need to be issued to satisfy the loan.

[8] It is of critical importance when considering the recoverability of costs from the plaintiff to assess what prospects the plaintiff has of recovering the advance from Parnell and St Stephens. That, in turn, depends on the overall financial strength of the two companies and their partnership. Both Parnell and St Stephens are in receivership as a result of default under the security agreement that they entered into with the BNZ. The evidence suggests that the total indebtedness of Parnell and St Stephens to the BNZ is $5,000,000. BNZ holds mortgage security for its advances. The properties over which the BNZ holds security have been recently valued. I should interpolate that in addition to mortgages over land the BNZ apparently also has security over a boat which seems to be generally accepted as being worth $400,000. The valuations of the real estate (which I shall call "the Parnell properties") were carried out by the firm Bayleys. One valuation dated 20 October 2009 values a house property at 43-45 St Stephens Avenue at $5,500,000. Another

estimates the value of two sections at $2,675,000. The total value of the property for which valuations have been obtained is therefore $8,175,000. If the valuations are regarded as accurate then after subtracting the approximate indebtedness to the BNZ there is an excess of $1,588,000. Mrs Fee for the defendants, however, did not accept that the valuations should be taken at their face value and I will return to that issue subsequently.

[9] In addition to the Parnell properties which I have been describing, Parnell and St Stephens also own an apartment which has been "e-valued" at $510,000. Parnell and St Stephens paid for the acquisition of this property by converting debt that was owed to them by the vendor, Fifer (Southern) Limited (FSL). To be more accurate, Parnell and St Stephens purchased the shares in FSL and the apartment was the only property owned by FSL. The net effect of all of these arrangements is that they have incurred a debt of $44,000 to the previous owners of the shares of FSL. If the "e-value" was correct, the equity of Parnell and St Stephens in the FSL apartment is $466,000, being the value of the apartment estimated in the "e valuation" less the $44,000.

[10] It would appear that the BNZ is prepared to release the securities which it holds over the three titles comprising the Parnell properties (and a boat) on payment of $5,000,000. Presumably such a release would follow on after re-financing had occurred.

[11] Mrs Fee, though as I have said, criticised these figures. She pointed out that the valuation of the Parnell properties was carried out on a willing but not anxious seller-buyer basis when Parnell and St Stephens are both in receivership with the BNZ holding security. Then she pointed out that the "e-value" of the apartment was not the subject of a formal certified valuation.

[12] My appreciation of the position is that if the valuations both for the Parnell properties and for the FSL apartment are market values, and if it is assumed that the probabilities are that those properties should be able to be sold on a willing but not anxious seller basis, then after deduction of liabilities there would be net assets available to Parnell and St Stephens of approximately $1,800,000, after deduction of

the advance from the plaintiff. If, however those properties were realised on a forced sale basis, there can be no such certainty. The valuations do not provide for a forced sale value. If a substantial discount were to be applied to the various valuations to reflect a forced sale, then the picture changes to one of net liabilities. Specifically, if a 1/3 discount is applied the shortfall of approximately $1,200,000 results –again after repayment of the advance from the plaintiff.

[13] I consider that it is appropriate to make an allowance for a forced sale given the following factors. First, the debt owed by Parnell and St Stephens is only as good as the financial prospects of those two companies which are in receivership. The existence of the receivership is an indicator of financial distress. Further, there is no indication in the affidavit evidence of any source from which current interest charges on the loans might be met. No doubt they are already attracting penalty rates. Further, while Mr Walker resisted this suggestion, I think there is strength in the defendant's contention that the fact that the affairs of both the plaintiff and Parnell and St Stephens are being managed in a coordinated way by Mr Paul Alexander, who is an undischarged bankrupt, adds to the risk factor. Moreover, there are other symptoms of financial constraint being experienced by other companies which the Alexanders are involved in.

[14] Further, there is uncertainty about whether the loan will even be recovered from Parnell and St Stephens. Mrs Fee asked rhetorically, why would the Alexander interests agree to the plaintiff calling up the loan, thereby transferring funds from one Alexander–controlled entity to another when the result would be that the money would be lost to the Alexanders and used to pay the costs award. I agree with those submissions.

Discussion

[15] I conclude that the "threshold" has been met. There is reason to believe that the plaintiff will be unable to meet an order for costs. That being so, the next issue is whether the Court in its discretion should make an order against the plaintiff. I bear in mind that there is no pre-disposition either way as to whether an order should be

made and that the exercise of the Court's discretion aims to balance the interests of the plaintiff and the defendant. In making an assessment, I am able to have regard to the merits of their claim. I do not intend to embark upon a further analysis, having carried out substantially the same exercise in the judgment that I gave dismissing the defendant's summary judgment application 31 August 2009. In that application I assessed the plaintiff's claim as being reasonably arguable. I take into account the fact that that where the prospects of success in a case are dubious, that will be a factor that will increase the chances of the plaintiff facing an order for security for costs: *Attorney-General v Transport Control Systems (NZ) Limited* [1982] 2 NZLR 19. But I accept that the plaintiff's claim in this case is not frivolous or worthless.

[16] Another factor which seems to be relevant to me is that it is not contended that making an order will have the effect of forcing the plaintiff to abandon its claim.

[17] Given the risks to the defendant, and the absence of any appreciable prejudice to the plaintiff that would follow from my ordering security for costs, my determination is that an order ought to be made.

Orders

[18] Having regard to the fact that the likely quantum of any adverse party and party costs award would be $75,000, the appropriate figure which the plaintiff ought to pay is $60,000. That sum is to be paid to the Registrar of the High Court at Auckland not later than 29 January 2010. The proceeding will be stayed until such time as the security has been paid.

[19] As to costs, the parties should confer and if possible agree on them, or alternatively I will hear counsel at 9 a.m. on a convenient date.

J.P. Doogue
Associate Judge