IN THE SUPREME COURT OF NEW ZEALAND
I TE KŌTI MANA NUI

SC 87/2018

[2019] NZSC Trans 10

**BETWEEN** **ROBT. JONES HOLDINGS LIMITED**
Appellant

**AND** **ANTHONY JOHN McCULLAGH**
**STEPHEN MARK LAWRENCE**
Respondents

Hearing: 30 April 2019

Coram: Glazebrook J
O'Regan J
Ellen France J
Arnold J
Kós J

Appearances: D G Chesterman and R P Nolan for the Appellant
B P Keene QC, L M Van and R A Idoine for the Respondents

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**CIVIL APPEAL**

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**MR CHESTERMAN:**
May it please Your Honours. Counsel's name is Chesterman, I appear for the appellant with my learned friend Mr Nolan.

**GLAZEBROOK J:**
Mr Chesterman, Mr Nolan.

**MR KEENE QC:**

May it please the Court, I appear for the respondent with my learned junior Ms Van and Mr Idoine.

**GLAZEBROOK J:**

Mr Keene, Ms Van, Mr Idoine. Mr Chesterman.

**MR CHESTERMAN:**

May it please Your Honours. Professor Farrar referred to a voidable transaction as in effect robbing Peter to pay Paul. This simple analogy really goes to the heart of the argument today. The heart of the issue. And that issue for determination is whether the common law rule that a voidable transaction must disadvantage creditors by diminishing the pool of company assets available to them, which I'll refer to as the disadvantage rule, applies to voidable transaction under section 292 of the Companies Act 1993.

Today I will address this argument over six submissions. The first is that the disadvantage rule is fundamental to voidable transactions and has applied since the inception of voidables law in the 1750s. The second submission, a fundamental common law rule, such as this, can only be extinguished by a clear and unambiguous statement of Parliament through legislation. It's submitted this has not occurred and that the Court of Appeal erred in finding that it had. This second submission goes to the heart of the appellant's appeal, and it's where most of the time will be spent.

The appellant says there are four reasons why the Court of Appeal was wrong. The first of those is the wording of section 292. The appellant says that does not, on its face, exclude the working of the disadvantage rule alongside section 292. The second reason the Court of Appeal was wrong is that the legislative material behind the 1993 reforms leading up to the enactment of section 292 shows that Parliament did not intend to extinguish the rule, nor did they raise any conflict between the rule and policies of simplicity, equal treatment or harmonisation. The third reason it is submitted the Court of Appeal is wrong is that the pari passu principle, which is the

principle of equal treatment, has existed alongside the disadvantage rule since the inception of this law, and has never been considered to be in conflict with it. In fact the two concepts work side by side which, in my submission, is that there must first be a diminishment before issues of equal treatment are even given rise to.

The fourth reason it is submitted the Court of Appeal was wrong, is that the disadvantage rule has been referred as the underlying rationale of the voidables regime in several New Zealand cases including one out of this court, *Allied Concrete v Meltzer* [2015] NZSC 7, [2016] 1 NZLR 141. So those all relate to the second submission, which is that the rule has not been extinguished.

The third overriding submission is that the Court of Appeal was wrong to uphold the case of *Levin v Market Square Trust* [2007] NZCA 135, [2007] 3 NZLR 591. That is the Court of Appeal authority that determined that the disadvantage rule no longer applied, and that was the first case to do so in New Zealand, to make it as a finding, and that was in 2006.

The fourth submission is that Australian case law should not guide the New Zealand position on the disadvantage rule, and the reason for this is that primarily the Australian position does not follow the Harmer Report. The Harmer Report was the Australian Law Commission's report into insolvency in 1988 and that is the report that the New Zealand legislature drew from in the 1993 reforms and when one looks at that report it is evident, in my submission, that it retained the disadvantage rule, and therefore Australian cases that say that the rule no longer applies, are against the very document that the New Zealand legislature moved forward on.

Secondly, the Australian position is inconsistent both under the old legislation, section 122 of the Bankruptcy Act, and under section 588 of the Corporations Act 2001. There are cases going both ways and the submission is the position is inconsistent and should not be followed.

The final submission is that the disadvantage rule will not cause practical problems and this is an issue raised by both my learned friends and the Court of Appeal. It is submitted that the rule existed for centuries without many or very few practical problems arising and that they are very unlikely to happen. Even if they do so in rare cases, and they will, that is not a reason for finding that the disadvantage rule no longer applies. That's an issue for Parliament to deal with. Now before –

**GLAZEBROOK J:**
Are you going to also explain why there is no diminishment in assets in this case?

**MR CHESTERMAN:**
Yes, just quite quickly simply it is a swapping of liabilities –

**GLAZEBROOK J:**
But not outside liabilities, outside of the group, is it?

**MR CHESTERMAN:**
I see where Your Honour – where Your Honour is getting to is in relation to MSH2 being a subsidiary of Northern Crest (NCI). So the submission is that the assets of Northern Crest were not diminished at all, and that one cannot look to the outside group as to diminishment of their assets, or issues outside the group, outside of NCI –

**GLAZEBROOK J:**
Well why not if they own them?

**MR CHESTERMAN:**
Well there are a couple of reasons. First, the legislature has specifically provided a mechanism for doing that, and that is a pooling application under section 271 of the Companies Act. So in –

**GLAZEBROOK J:**

But that’s nothing to do with preferences is it? I just want to know why there’s not a diminishment. You say you just look solely at Northern Crest, is that the submission?

**MR CHESTERMAN:**

That’s right, and it might be better, that is my submission, you look solely at Northern Crest, you do not go beyond the group of the wider Northern Crest pool, and both case law –

**GLAZEBROOK J:**

And why would you do that, in this type of situation? Why would you say there’s no diminishment because we’re swapping one liability for another and just ignore the fact that part of the assets of the parent company are the shares in the subsidiary?

**MR CHESTERMAN:**

Because these are, one of the principles that applies in voidable transaction law is that you give respect to the legal entities involved and the fact they are –

**GLAZEBROOK J:**

But I'm just talking about its property. Its property is the shares in its subsidiary.

**MR CHESTERMAN:**

Well my submission here is that we are looking at the pool of assets of Northern Crest and as for its property being its shares in its subsidiary I'm unaware how they would be factored into the total –

**GLAZEBROOK J:**

Well it certainly wasn’t going to be repaid, was it, the debt?

**MR CHESTERMAN:**

Excuse me Your Honour?

**GLAZEBROOK J:**

The debt wasn't going to be repaid, was it?

**MR CHESTERMAN:**

By who?

**GLAZEBROOK J:**

Northern Crest.

**MR CHESTERMAN:**

Well I understand that it was, Your Honour, because MSH2 applied to be a creditor in Northern Crest's liquidation.

**GLAZEBROOK J:**

There wasn't any money, though, as I understand it.

**MR CHESTERMAN:**

Your Honour, this is an extremely important issue, and I'm glad you've raised it first. I address it in some detail in my fifth submission, which is once I have gone through –

**GLAZEBROOK J:**

If you're going to address it later we'll come to it then.

**MR CHESTERMAN:**

Yes I address it later.

**GLAZEBROOK J:**

I was going to say, too, that we don't need to go through in great detail the history, we have read the submissions. We want to concentrate on the, section 292 and the wording and I note you are coming to that.

**MR CHESTERMAN:**

Yes. So before I move on to that I want to just address some housekeeping issues, which I thought I'd do at this stage before I start into the submissions. I provided some further volumes and I just wish to explain what they were. Volume 5 was a bundle of debates and it simply replicates the debates that were already provided originally, except that this provides tabs and indexes so they'll be easier to go to when we need to and it will save time during the submission. The, volume 6 was also provided, and that is also a replica of material already provided. It's a legislation bundle and it divides it into tabs and is paginated and will make it quicker to refer to these documents.

The seventh bundle that was provided provides case law and three of, well most of those cases are merely just cited in authorities already provided. For example, authorities 1 and 3 were referred to *Lewis v Hyde* [1998] 1 NZLR 12 (PC). *Williams v Murdoch* [1968] NZLR 1191 (SC) is referred to in the *Laws of New Zealand* and Carter on Statutes referred to *Kumar v Station Properties Ltd (in liq and in receivership)* [2014] NSC 146, (2014) 15 NZCPR 548. And then in terms of the secondary materials I provide a copy of Carter, which the respondents have already provided part of, some further excerpts from report number 9 from the Law Commission, and a document from the Ministry of Economic Development, which we only just obtained after a few months of asking for, but that is referred to in *Allied Concrete* at paragraph 42. So all of these documents in bundle 7 are just coming from material that's already been provided, and provide a more complete version of that. However, my friend did raise an issue with me at the start of the hearing, which is why I've taken you through those, and he may well raise that as a problem. I have a bundle of further –

**KÓS J:**

Sorry, what sort of problem?

**MR CHESTERMAN:**

My friend's issue was that he had been provided material at the last minute and so I went through the volumes with him and explained to him what I've

just explained to the Court, and it seemed that he was okay with that, but perhaps after I've spoken he may take a different view.

**KÓS J:**
Right.

**O'REGAN J:**
Wouldn't it have been easier just to provide it at the outset so that we're not looking at two different – we've all read stuff from the stuff you've already given us, now you're going to take us to something else.

**MR CHESTERMAN:**
You're absolutely right Sir, it would have been, and I apologise for that.

**GLAZEBROOK J:**
Can we just perhaps check if Mr Keene did have a problem with anything?

**MR KEENE QC:**
Until this morning I didn't have an understanding of what the content of the documents were. The documents were quite long and non-specific and my concern was that we would be blindsided because we only received these after the close of business on Friday. So I had intended, and notified my friend, that if, as he presents his submissions, I feel that anything that has come through in this latest set puts me at a disadvantage, I may ask the Court at the close of my submissions to have the ability to respond to those things. I haven't looked at it in any real thoroughness. As has been presented so far, we're not taking any objection, but we do feel that that is something that might turn up and we'll see what happens.

**GLAZEBROOK J:**
Maybe what we need to do is to make sure we've got references both to the new bundles and to where it is in the old bundles, and then Mr Keene won't be at a disadvantage because he can reply based on his old bundles that he's familiar with, and actually that applies to the Court as well, to a degree. So

just explain where the material is in both sets of bundles if you would Mr Chesterman.

**MR KEENE QC:**

Ma'am, while I'm on my feet, I also indicated to my friend that the maximum amount of space that ought to be taken with the oral submissions is three pages and he's gone to five. If I'd known there was leave to go to five, I might've gone to five myself.

**O'REGAN J:**

Believe me, it doesn't advantage you to put in long oral submissions, so you're better off where you are.

**MR CHESTERMAN:**

Before I comment I have some further material to hand up. Mr Nolan will hand it up to you and then I'll just take you through it. So the first document is a copy of the filed submissions, but it's annotated with bundle references. You have a hyperlink version but the document that was filed, the hard copy, didn't have the bundle references so this copy has those if you want them, but it's unnecessary if you're using the hyperlink. The second document, annexure A, is commonwealth voidable preference legislation, and this provides a comparison of the legislation in various jurisdictions setting out the essential passages within the legislation and then the second part of it describes which of those have an intention requirement and which do not, and finally the different clawback periods in each jurisdiction.

The third document that you have is a copy of the appellant's synopsis of oral submissions. I do apologise it went to five but I would say at least two of it are the authorities referred to in it, so there's really not much in it in terms of content.

The next document is a situation chart. Now one of the issues raised by the respondents were a number of different practical examples where the diminishment rule would cause problems and so what I have done is just

prepared a response to that by setting out a number of different situations like bank overdrafts, secured loans that sort of thing, and the position in the, if diminishment is required, as compared to if it is not. And I've provided that simply because there is limited time today and it may be an issue that, in my submission, it's not highly relevant to the appellant's case today because if the rule has not been extinguished then in my submission it's not relevant that there might be practical problems, but in any case I've addressed those.

The final document again is to save on time today if necessary. The respondent refers to the Australian position and what I've simply done is just set out chronologically the cases referred to by the appellant and the Court of Appeal and the respondent chronologically so that the Court can see where intention has been – sorry, where the disadvantage rule has been held to apply and where it hasn't.

Thank you, I think the appropriate starting place, Your Honours, is to go section 292 and if Your Honours take bundle 6 at tab 14, the relevant provision is section 292, it starts at the bottom of page 28, and the focus of today's argument is on the next page at subsection (2)(b) and it's, "An insolvent transaction is one that enables another person to receive more towards satisfied of a debt owed by the company than the person would receive, or would be likely to receive in the company's liquidation." The submission for the appellant is that the wording of this section 292 as a whole, but in particular those provisions, do not work to extinguish the disadvantage rule and that, in fact, the disadvantage rule can work side by side with those provisions.

Before I move on also it's relevant to go to the predecessor to section 292, which was section 309 of the Companies Act 1955, and that is at tab 12. The reason it's important to go to this provision, and to look at its wording, not just because it was the section immediately in place before section 292, but it's because it sets out what the changes were that the legislature intended. So if we look at section 309(1)(a) a voidable transaction, "It is in favour of any creditor … with a view to giving that creditor or any surety … a preference …"

Now those were the words that caused a lot of issues with voidable transaction law in that it set out an intention element, and it was very difficult for liquidators to prove a voidable transaction because they had to subjectively look at the intention of the company with paying the debt and there were other requirements such as if they were pressured into paying a debt that could negate intention, and it really made the scheme unworkable. So when we get to the material, which I'll move onto promptly, given that I understand that you're familiar with the background, when you move onto the material that's quite clearly, in my submission, what Parliament is addressing, the removal of this intention requirement, which is set out in the section, and you'll see that in section 292 the words "with a view" no longer exist, and it might actually help at this point if I just review the international legislation.

**KÓS J:**

Well before you do that, the change at 292(2)(b) from 309 is very much more than simply getting rid of "with a view".

**MR CHESTERMAN:**

Yes, you're correct Your Honour, yes. I'm sorry for interrupting.

**KÓS J:**

No, the focus is plainly now on the effect on the preferred creditor.

**MR CHESTERMAN:**

Yes, that is the precise wording used by the Commission and in the Parliamentary debates was a removal of the focus from the intention of the company to the effect of the transaction.

**KÓS J:**

Yes.

**MR CHESTERMAN:**

And it's really, I suppose, as Your Honour has done well to signal that point, is that it's that the words what do they mean by on the effect of the transaction

and the submission for the appellant is those words focusing on the effect of the transaction, were not meant to exclude the disadvantage or the diminishment rule, but in fact retained it. However, those words have been interpreted, for example, by Justice Randerson in *Chatfield v Mercury Energy* (1998) 8 NZCLC 262,645 as meaning that the section was no longer concerned with the ultimate financial effect of the transaction and my submission is that interpretation was wrong and that when the legislature were focusing on the effect, that was simply to be understood, well we're no longer concerned with intention and subjective decisions and pressure, we're now just going to look at the transaction itself and its effects, and so my submission is that the disadvantage rule is completely consistent with that focus that was intended and the legislature did not, of course, state the disadvantage rule in the new section 292. What happened with the reforms was that there was, in my submission, not a complete codification but a partial codification of some element of, major elements of voidable transaction law, but there were a couple of areas that they didn't address. An important one of those was third party transactions because of the new section 292 just says payment by the company and the authors Heath and Whale comment that if one just looks at those words strictly and, in my submission, apply a plain meaning approach, a literal approach, as the Court of Appeal has done in this case, then third-party transactions would not be covered. But the common law has filled that gap, as it should, in certain circumstances and said that certain third-party transactions are captured so –

**O'REGAN J:**

I don't think it's the common law it's just the way the section has been interpreted. If somebody makes a payment on your behalf it's a payment by you. That's not the common law, that's just the Court saying that's clearly what the section was meant to cover, and in this case where you have a disadvantage, where you're looking at the impact on a creditor of advantage, which you've accepted is what the section focuses on, in this case your clients got $260,000 and everybody else got nothing. Why is that not a disadvantage – why is that not an advantage to your client?

**MR CHESTERMAN:**

With respect Your Honour I haven't accepted that the focus is advantage. My submission is that disadvantage is required by the section.

**O'REGAN J:**

I know that but you're saying that the focus, that the switch from section 309 was to get away from intention, to look at the effect on the creditor.

**MR CHESTERMAN:**

That's right.

**O'REGAN J:**

In this case the effect on the creditor was a $260,000 windfall that nobody else got. Why is that not what the section is meant to cover?

**MR CHESTERMAN:**

Well because, Your Honour, the other creditors were not disadvantaged. They were in the same position before the transaction as they were after. Let's look at it this way. If immediately before that payment Northern Crest was liquidated –

**O'REGAN J:**

That would also have been true if the cheque had been written on an overdrawn account. I mean there's umpteen ways you could argue that, but that would mean basically – I mean on your argument the section would effectively never apply. You've said in your submissions, unless there's a reduction in net assets then section 292 doesn't apply but there will never be a reduction in net assets because if you pay a liability out of your assets both of them come down by the same amount and the net asset position stays the same. So when would it ever apply?

**MR CHESTERMAN:**

Well Your Honour the, and perhaps that's my fault in terms of the wording, but I thought it was clear in the fact that the appellant didn't appeal against the

Columbus payments. It's not its position that you look at a balance sheet analysis where there's a zero impact on the balance sheet which is the net effect –

**O'REGAN J:**
Well just go to paragraph 10 of your submissions, your question is, "Does the common law requirement that an insolvent transaction disadvantage the pool of creditors by decreasing the net assets of the company," that's the way you frame what you say is the common law rule, and if that is the common law rule section 292 would never apply.

**MR CHESTERMAN:**
That is perhaps a – first of all the position is that by the word "net assets" it's simply looking at the assets not at a balance sheet of assets and liabilities from an accounting perspective.

**O'REGAN J:**
Well that's not net assets then.

**MR CHESTERMAN:**
In terms of an account – well.

**O'REGAN J:**
Net assets are assets netted off against liabilities and in this case if you're talking about net assets when you're dealing with the point of view from creditors, you're never going to have a reduction in net assets.

**MR CHESTERMAN:**
Well I can answer that quickly Your Honour. I'm not talking about a balance sheet net asset position, and you're right, because if that was the case then the no asset, no transactions would be voidable, and it's clear that the appellant is not saying that because it did not challenge the Columbus payments which were much greater than the MSH2 payments. They had a zero effect on the balance sheet but they're not being challenged.

**O'REGAN J:**

Well shall we cross out the word "net" in your paragraph?

**MR CHESTERMAN:**

Yes, cross out the word "net". The position is that you look –

**GLAZEBROOK J:**

So the assets are not diminished, is that the –

**MR CHESTERMAN:**

Yes, you look at the asset pool and whether that has been diminished.

**ARNOLD J:**

Can I just ask something that slightly puzzled me, and it's addressed I think in your situation number 1. Is it a key of your argument that the payment from the lender went directly to Robert Jones and not through the company?

**MR CHESTERMAN:**

Yes.

**ARNOLD J:**

And yet it's the company who's directing the payment to Robert Jones. So to understand it, if the payment had been made to the company, and the company then made the payment to Robert Jones, you accept that it would be caught as a preference?

**MR CHESTERMAN:**

Yes, if that payment was made into the company and was available for the creditors, then yes it would be voidable. If I may expand upon this answer Your Honour. The voidables regime looks at transactions and their form and substance. The transaction in this case is a payment from MSH2 direct to Robert Jones. There's no loan contract. The payment simply happened and it was deemed by the experts through accounting entries after the fact to be treated as a loan. Now in terms of that loan contract that existed, the

fundamental term of that, well, an essential term of it is that the payment goes to Robt. Jones Holdings. If a court or –

**ARNOLD J:**

But whose requirement is that, that's the company's, the borrowers requirement?

**MR CHESTERMAN:**

If I just may develop this point, MSH2 is a separate legal entity and it can do with its money what it wishes. If it agrees with the company to pay that money to a specific creditor directly, that is a matter for MSH2. However, to say that that is an equivalent payment to the company in my submission is inventing a new transaction that never occurred. if one takes that principle further that would mean that it gives the liquidator, it injects them into freedom of contract between the company and third parties, just putting to one side that this was a wholly owned subsidiary, it's still a separate legal entity. So if the liquidator can jump in and say any payment by a third party could have gone into the company, in my submission, that is inventing a hypothetical –

**ARNOLD J:**

Or any payment by way of a loan to the company.

**MR CHESTERMAN:**

Yes.

**ARNOLD J:**

That's the critical part to my mind. What you're talking about is almost entirely a matter of form. If the borrower says to the lender could you pay it directly to X, for myself at the moment I don't see why that isn't a sum that the company has, it's the company's money, and it is simply directed where it is to go to.

**MR CHESTERMAN:**

Because the facts, or the evidence in this – in a situation perhaps where there was a loan agreement between the company and the lender, and that gave

the company access to funds, cash to do with what it wanted, and it then said, following the signing of this contract, said to the lender, this money that we have for our availability, instead of paying it to us pay it to the creditor. So that would be a different situation from what we have here because there was a loan contract in place which identified that it was the company's money and the test, this is important to keep in mind, assets of the company available for the creditors. Now my submission is that it's a different situation if there is a contract with a third party, or an undocumented contract, where the third party agrees to pay money to a third party. It is, that is the substance and form of the agreement. Nowhere in that agreement is there any agreement by the third party to pay that money into the company to do with what it wants because the company might have said to the third party, pay it into our bank account, we're going to spread it among ourselves, we'll do what we want. The third party could quite equally say no because the third party is a separate entity, it's its money, it can do with what it likes, and to create a situation where you say that any time a third party pays a creditor on behalf of a company, that is the company's money, in my submission is creating an evidential presumption, it is, an evidential presumption is necessary because that conclusion of what occurred, that it is the same as a payment to the company, is a different contract, a different scenario and a different transaction and my submission is that that evidential presumption is not legislated, and it's not supported by policy or the Act, and I suppose that goes to the – I'm glad Your Honour asked that question at this point because it really does go to the heart of it, which is was this payment an asset available for the creditors, and on the evidence before us my submission is it cannot be, and the only way it can be is if the Court injects, allows an evidential presumption to exist, and if the Court allows that, then where does it end. Does it, I mean of course we can say, well it's confined to voidable transaction cases but why should a liquidator have that power over a third party's money to say you should have or could have paid it into the company.

**GLAZEBROOK J:**

Can I just make sure I'm on the same page. So, in fact, you're not arguing for there being no diminishment of assets because you accept that if the

company borrowed from the bank 260,000 and then paid out Robert Jones, that in fact that would be a preference?

**MR CHESTERMAN:**

Yes, and can I – because the money would then increase –

**GLAZEBROOK J:**

Right, so it's not a general diminishment argument at all, it's saying that if the money never went to the company, then there were no assets available. So it's actually totally different from what Lord Mansfield was talking about, if I understand your submission.

**MR CHESTERMAN:**

No, in my submission, not Your Honour. It is identical to what Lord Mansfield was talking about. If that money becomes available for the creditors, the asset pool is then increased by whatever that money is. Forget about the liability. The assets available for spread are then increased because there's more cash that can go to all the creditors, and then, remember we're just looking at the asset pool, when that money is –

**GLAZEBROOK J:**

So this is an incredibly narrow case, which actually I'm sure if we'd realised we wouldn't have given leave.

**O'REGAN J:**

I don't think that can be right. I mean if the company paid Robert Jones out of an overdrawn account, surely that would be, your argument would be that that wouldn't lead to any diminishment either. It just further went into debt with the bank, wouldn't that be the case?

**MR CHESTERMAN:**

It would not be diminishment because there you are simply swapping one creditor for the other. One unsecured creditor for the other.

**O'REGAN J:**

So the difference is if you go to the bank and say, can I borrow money from you, and the bank says yes and gives it to you, and then you pay it, that is a preference, but if you go to the bank and say, can I increase my overdraft, and they say yes, that isn't a preference. I mean surely that's just dancing on the head of a pin?

**MR CHESTERMAN:**

I don't believe it is Sir. It's just applying –

**GLAZEBROOK J:**

I don't understand the overdraft business sorry, I'm totally lost now.

**O'REGAN J:**

Because you've never had the money, you've just gone further into debt.

**GLAZEBROOK J:**

Okay.

**MR CHESTERMAN:**

It has never been – it's helpful to look at these from the hypothetical perspective of a liquidation. So if the company is liquidated immediately before the bank overdraft is used to pay the creditor, the liquidator is not going to, or can't, access that overdraft to start paying creditors or bills, it's not an asset of the company available. So when you focus on the total pool of assets, the argument does become –

**O'REGAN J:**

So how would the liquidator even know this? If the company won't give its records, how would you work out whether when a payment was made the account was slightly in overdraft or was slightly in positive territory, because that would be crucial on your argument as to whether it was a preference or not. So a company writes a cheque to me for $100, when the account's got $100 in it, that's a preference. Then it writes one to you, which puts the

account $100 into overdraft, you would say that's not a preference. How would we know that, how would we know which cheque, when the company was in overdraft and which cheque wasn't?

**MR CHESTERMAN:**
Well, Sir, there will always be, as we've seen from the existing system without the disadvantage rule there are complications, and Your Honour has just mentioned one now, and –

**O'REGAN J:**
But isn't it easier just to forget about it and say it doesn't matter. That's a much fairer outcome, isn't it. You and I both received $100, we both received it on the same day, why should one be different from the other. Why should we impute an intention to Parliament to create this incredible level of complexity, and on the face of it unfairness and capriciousness, when we don't need to.

**MR CHESTERMAN:**
Well with respect Your Honour I'm not asking the Court to impute a new principle to Parliament, I'm asking the Court to reinstate a principle that is centuries old that in my submission –

**O'REGAN J:**
Yes but Parliament changed the law. That's yesterday's news that law. We've got a new law now, it says what it means, it means what it says. Why do we have to go beyond that?

**MR CHESTERMAN:**
Well, Your Honour, we have to go beyond it and perhaps it might assist if I move on to what happened with the changes. We have to go beyond it because it was a fundamental rule of voidable transaction law right up until 2006.

**O'REGAN J:**

Well can you point me to a case under the old law where a payment was found not to be a preference because the account happened to be in overdraft at the moment that the payment was made. I mean was this really the way the law worked in the past?

**MR CHESTERMAN:**

If Your Honour –

**O'REGAN J:**

Are there any cases, I couldn't find any?

**MR CHESTERMAN:**

Well in *Lewis v Hyde* I think it sets out what the Privy Council –

**O'REGAN J:**

But *Lewis v Hyde* –

**MR CHESTERMAN:**

May I just answer Your Honour?

**O'REGAN J:**

– was a case where no preference happened.

**MR CHESTERMAN:**

*Lewis v Hyde* the Privy Council said there was not, there was no previous case law on the issue because it was so basic and such common sense that it had not come before the Courts, and what the Privy Council did in that case was they referred to obiter in a number of older English decisions, but they also referred to obiter in some New Zealand decisions, and of course they upheld the Court of Appeal, and those decisions talked broadly about disadvantage to the creditors being required, a situation where the payment is at the expense of the other creditors as I mentioned in my opening example, robbing Peter to pay Paul. So my answer is no, there are not these cases,

and the reason that there’s now, I would presume, is because the intention requirement within the law that existed up to that point made it extremely difficult for these cases to succeed but also, as the Privy Council pointed out, it was a basic rule which they described as common sense. Would it assist Your Honour if I took you to the passages in *Lewis v Hyde*, I wasn’t going to?

**O’REGAN J:**
I've read it. I'm familiar with the passages.

**MR CHESTERMAN:**
So the primary one is at page 18 Your Honour. I'm not going to take you through it but just give me one moment.

**GLAZEBROOK J:**
Well you might as well take us through it if you’re going to read it.

**MR CHESTERMAN:**
So that’s volume 2, tab 18, and it’s the second to last page of the case, the lines 30 downwards, and there the Court first of all talks in the context of whether an actual preference is required and talks about the fact that section 309 did not state actual preference as a requirement, and by actual preference they are referring to disadvantage to creditors, and that is apparent when we look at the Court of Appeal decision. The very last paragraph is relevant. “The result conforms with the common sense of the matter. There is no reason to set aside a transaction so as to bring assets into the pool of assets available for distribution amongst creditors in the insolvency unless the transaction so set aside has in fact diminished the pool which would otherwise have been available.”

If we go back one page to page 17 and at the top of the page again it just states that, “Far from bringing back into the pool moneys which would, apart from the preference, have been available for pari passu distribution … the effect would be to increase the pool by recovering moneys which would not, in any event, have been so available.” Then the Court says, “It is probably this

basic consideration which accounts for the fact that Their Lordships were not referred to any decision or textbook where the point has been directly raised or argued." And then their Honours refer to an English case and then the Court of Appeal in *Tyree Power Construction Ltd v D S Edmonds Electrical Ltd (in liq)* [1994] 2 NZLR 268 (CA), which was one of the additional authorities that I provided.

It may also be helpful to just briefly look at the Court of Appeal decision which was upheld by the Privy Council and that's at tab 16, and I'm referring Your Honours into the second page of that case on the, we'll start just near the top of the far right column, referring to *G & M Cook Ltd (in liq) v Savoy Restaurant Ltd* (1982) 1 NZCLC 95-059 (HC). I provided that case in the extra bundle, and there they talk about the concept of, "What is meant by a preference is the giving to one creditor of an advantage over the other creditors, thus preventing the equal distribution," and then if we go down to paragraphs beginning, "The apparent objective of s 309 was to prevent preferences which resulted in disadvantage to other creditors."

So it was, that's how the Court of Appeal addressed it and there was one further authority, which is in the same bundle at tab 20, and that is *National Bank of New Zealand v Coyle* (1999) 8 NZCLC 262,100 (HC), that is the authority that was overturned by *Levin* and the relevant part of *Coyle*, which is at tab 20, that's the right side of the page, left column. It's page 262, 103, it's the second page in on tab 20, and unfortunately the hole punch has punched through the numbers at the top but it's the second page of the case on the right-hand side of the page, and there's a heading on the left column of the right side, "Did the bank receive more," and in this situation what happened was a shareholder, three shareholders paid off part of a bank overdraft and it was considered that that was just swapping in their liability for another and it was argued there was no diminishment and Justice Panckhurst on the left column at the bottom said, "The first argument puts in focus the very nature of the voidable transaction regime." Then he describes a transaction at the top of the right column. "An injection of capital by way of loan to the company, its asset position did not alter. To the extent that the

company's indebtedness to the bank was reduced, it incurred a corresponding liability." His Honour then refers to *Chatfield v Mercury Energy* which is the decision relied upon in *Levin* which by the way is an ordinary course of business case. it wasn't actually dealing with the issue of diminishment at all and refers to the passage in *Chatfield* and then His Honour reaches a conclusion about whether or not this supports the proposition that dissipation of the company's assets is no longer required. "With respect I doubt that it is appropriate to go so far. Unquestionably the old test of subjective intention to prefer has been cast 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." Then His Honour refers to *Lewis v Hyde* and to their reference to diminishment being a universal assumption that actual preference was required, and there's that linking of the phrase actual preference –

**KÓS J:**
Sorry, where does diminishment appear in that? The preference, actual preference is the universal assumption but…

**MR CHESTERMAN:**
Yes, so when, in this case, in both cases actual preference is used as a way to describing a situation in which other creditors had been disadvantaged and disadvantaged by a diminishment of assets. Now when I took Your Honour to the last paragraph of the Privy Council of *Lewis v Hyde*, that's where they explain that, prejudiced by diminishment of assets in the pool, and so His Honour then refers to *Lewis v Hyde* and concludes on the next page that His Honour is of the view that the reasoning is still of equal application and the 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…"

**GLAZEBROOK J:**

But wasn't this a case where a loan did come into the company, which you now say wouldn't cause a, would cause a –

**O'REGAN J:**

No, they made payment directly to the bank, didn't they?

**MR CHESTERMAN:**

They did, yes. That money was never paid in for the general pool.

**O'REGAN J:**

So you'd say it's analogous with this case?

**MR CHESTERMAN:**

Yes.

**GLAZEBROOK J:**

But it's not a distinction that was actually made in the reasoning at all is it? That's what I'm having difficulty with. Your distinction that you're making doesn't seem to be a fundamental aspect of any of the reasoning about diminution of assets.

**MR CHESTERMAN:**

Your Honour, I was going to –

**GLAZEBROOK J:**

So it seems to be a gloss, is what I'm saying, that you're now adding, that didn't seem to exist in the reasoning of the cases.

**MR CHESTERMAN:**

I can't say anything more Your Honour than I submit it's not a gloss it's just a more in-depth explanation of what the rule is about, which is that you look at the pool of assets themselves and have they been decreased and it's really, in my submission, a relatively straightforward principle when you look at these cases, for example, in *Levin v Market Square Trust* what happened there was

the, although in that case, that was the case that held that the disadvantage rule no longer applied to section 292, what occurred in that case is that the lender gained security for the loan, so you weren't swapping an unsecured creditor for an unsecured creditor, you were swapping in a secured creditor for an unsecured creditor and that money was going to be dealt with by the sale of the business and His Honour Justice Kós referred to this case in one of his recent decisions out of the Court of Appeal which is *Ebert Construction Ltd v Sanson* [2017] NZCA 239, [2017] NZCCLR 28 and at paragraph 41 of that judgment His Honour referred to two cases which he considered were straightforward as to why they were voidable. The first was a case called *Westpac Banking Corporation v Nangeela Properties Limited* [1986] 2 NZLR 1 (CA) where the company sold a building and used that money to pay a creditor. So in that case clearly you have an asset that has been diminished and His Honour also said that the *Levin* case is straightforward as well, and it is, because for the same reason, you've got a secured creditor swapping in for an unsecured one so the pool of assets for the unsecured creditors is then diminished. So my submission is it's not an artificial gloss but it's simply just an explanation of how the rule applies in practice.

I intend to go, perhaps one of the most important of today's submission –

**GLAZEBROOK J:**
But your submission is that if an unsecured creditor swaps in for a secured creditor, that the money goes into the company, then there's a diminishment of assets, but if the unsecured creditor pays directly then there isn't a diminishment in assets. That's what I understand your submission to be which –

**MR CHESTERMAN:**
No, no, in the Robt. Jones case you have an unsecured creditor switching in for an unsecured creditor. The asset pool is untouched. No money has gone out of the company. If there is cash in the bank, it's identical to what it was before the transaction, for all of the unsecured creditors. The situation is different if you have a secured creditor switching in for an unsecured creditor

because then although there's been no cash added to the company's pool, part that cash available for the unsecured creditors is then diminished by the amount that is made available for the secured creditor that switches in.

**ELLEN FRANCE J:**
I must say I'm struggling a little bit to understand the distinction that you're trying to make. What's the policy reason behind that? The distinction that you're drawing?

**MR CHESTERMAN:**
The policy reason, Your Honour, is that the purpose of the voidables regime is to protect against diminishment of assets. It's an underlying requirement of the, it's why the regime exists. There is the policy of equal treatment and simplicity, we can go to those, but this is the very underlying mischief that the entire regime was created for to make sure that the pool available for the unsecured creditors remained the same. So another issue that comes up when looking at this is, you know, issues of fairness and equality and the Companies Act is about companies, it's about commerce and money. If a creditor is in the same position before a transaction as they are after, you've got the same amount of money for them in the pool of unsecured creditors, but one of them gets paid off, why should they mind? The only reason they'd mind is they think it's unfair. It's unfair in perhaps a strict moral sense but from a commercial, financial sense, they are in an identical position before as after, and my submission is that when you look at this concept of equal treatment aspects like that, it is purely in the sense fairness or morality in the terms of how it affects the bottom line, the dollar, because you cannot divorce this concept of fairness and equal treatment from the fact that it must be at the expense of the general creditors. They should only care, and the liquidator should only care, if that pool has been decreased.

**KÓS J:**
First of all it's not simply about money, Mr Chesterman, it's about assets.

**MR CHESTERMAN:**
Yes.

**KÓS J:**
Secondly, I have some difficulty with the overdraft distinction which you seem to be drawing in your discussion with Justice O'Regan and thirdly, all of this seems to have a slightly surreal quality to me, because if we are talking about assets, and circling back to the question that Justice Glazebrook started the hearing with, I still don't understand why there has to be a diminution assets here, in as much as MSH2 appears to have been a wholly owned subsidiary, it paid the money to Robt. Jones out of what appears to be revenue, so therefore it was cash available to that company. If it was available to MSH2 it would have also been available to the creditors of its parent company Northern Crest. At some point we're really going to have to address this point because we're sort of putting off the inevitable if you want your argument number 4.

**MR CHESTERMAN:**
Well, sir, if there was a contract between the two companies concluding that MSH2's money was available for Northern Crest, then I would agree with Your Honour, but that's not the case here. In the High Court Her Honour Justice Gordon found paragraph 145 that MSH2 was not Northern Crest's treasurer, so that was the evidential finding, and that was the argument run by my learned friend as to why there was this access to the money.

**KÓS J:**
No but it was Northern Crest's vassal, it was under the control of Northern Crest.

**GLAZEBROOK J:**
So if it wanted the money, and it needed the money from its subsidiary, it could wind up the subsidiary and get the money. So it has to be an asset in the sense of the shares are an asset.

**O'REGAN J:**

Only if there weren't creditors of the MSH2 that ranked ahead of Northern Crest's shareholders.

**MR CHESTERMAN:**

With respect, how far does this go then? So the, does this extend the liquidation regime, which is looking solely at transactions, to the wider company group and situations where there's no finding that the subsidiary is a treasurer, no contract between the two that one has to pay, and so the third party has to pay the company's debts, so does the Court just jump in, and where does this take us. Should not the voidable regime, in my submission, just be limited to the transaction and the company that it relates to, because it's already wide enough. In my submission, New Zealand has the widest voidable transaction regime out of any of the jurisdictions that I've mentioned by being able to go back two years to any party regardless if they're related or not. Other jurisdictions do not allow that. They're between three and six months for every creditor but if you're a related party then different provisions kick in.

It might assist the Court if I, at this stage, skip to my third submission to take Your Honours to some commentary on the points that we've been discussing and then I will come back to the legislative development of section 292 because once I take you to this material then at least Your Honours will understand the basis for my submission and then we can move on from that and leave it as a matter for Your Honours to deal with.

So I'm going to ask you to take bundle 4 and go into tab 7 and this is a UK text by Parry, *Transaction Avoidance in Insolvencies*, and if you turn into the second page, page 164 at the bottom, and the heading at paragraph 5.51 "Disadvantage to other creditors" and –

**GLAZEBROOK J:**

This is under an intention-based regime, isn't it?

**MR CHESTERMAN:**
It is Your Honour.

**GLAZEBROOK J:**
Because one can understand to a degree that in an intention-based regime, because it's looking at what the intention of the payer is, that it might be different from looking at it from the other side. Because if your intention is to pay someone but not to diminish the assets then one can understand perhaps more that diminution argument and most of the comments relate to intention-based regimes, as I understand it, although you say some don't.

**MR CHESTERMAN:**
Yes and I –

**GLAZEBROOK J:**
And I think you've given us the references for that, as I understood you at the beginning.

**MR CHESTERMAN:**
My understanding of the commentary, Your Honour, is that with these intention-based regimes they are looking at an intention to prefer to put one creditor over the others but the cases that I referred you to, *Lewis v Hyde*, what they're saying is that it's a basic underlying requirement to that, to any voidable transaction, that there be a disadvantage to other creditors, a diminishment, and so I do not link the advantage/disadvantage test with an analysis of intention. My submission is they are completely different analyses and that the disadvantage rule is looked at as an underlying feature of a voidable transaction that must happen before you then look at intention. So that's my response to your distinction point Your Honour.

**GLAZEBROOK J:**
I suppose my difficulty is understanding the new distinction you're now putting on that, because I can understand a distinction that says, well, if you swap one debt for the other, however that happens, then there isn't a diminishment

in assets, but I can't understand, nor do I understand the previous cases as making a distinction between an overdraft, a loan that comes in and a third party transaction, which is, as I understood it, what you're doing.

**MR CHESTERMAN:**
So let me take you through, there are three different commentaries and –

**GLAZEBROOK J:**
Well do any of them make the distinction you're now making?

**MR CHESTERMAN:**
Yes, let me take you through them. There are three commentaries. There's one case and hopefully then I will have, they will have addressed the issues. So if you turn into the next page, 165.

**GLAZEBROOK J:**
I must say, this is a terrible photocopy, at least the one I've got is.

**MR CHESTERMAN:**
My apologies Your Honour. I could, if it would assist we could provide a better copy for you –

**GLAZEBROOK J:**
Well I'm not quite sure why it's come out the colour it has because it makes it very difficult to read.

**MR CHESTERMAN:**
I'll read it out for you Your Honour. This is at the top of page 165. "Where a transaction has no impact on the debtor's estate. For example, where a creditor is paid using sums provided by a third party in circumstances where the payment has no effect on the entitlements of other creditors, should this mean that the payment is not a preference? The payment would advantage the creditor receiving it, but it would have no effect on the debtor's estate unless the third party that provided the funds had a secured claim against the

debtor for reimbursement, or owed money to the debtor company and paid the creditor in discharge of that liability. Absent an effect on the debtor’s estate, the payment would cause no disadvantage to other creditors: the creditor’s unsecured claim against the debtor would simply be replaced by the third party’s claim against the debtor for reimbursement.” It then refers to a case, *Hawkes Hill Publishing Co Ltd*, which establishes that point but I haven't provided it because the facts are slightly different in that the creditor has security.

It then goes on to discuss that case. “This approach suggested that in a case where was no disadvantage caused to the other creditors the payment would escape avoidance.” Then it refers to in contrast *Re Sonatacus Ltd*, “A preference was found in circumstances where the payment made by the debtor had no net effect on the debtor’s balance sheet, since a liability of a value equivalent to the amount of the payment was discharged. This is logical since in those circumstances the assets under the transaction would otherwise have been available for unsecured creditors. As a result, the mere fact that the transaction had a zero impact on the debtor’s balance sheet is not fatal to a preference claim and what matters in such cases is whether there is a disadvantage to other creditors.”

The author then goes on to refer to an Australian authority which I will address later which is *G & M Aldridge Pty Ltd v Walsh* [2001] HCA 27, (2001) 203 CLR 662, in which the Court found that payment to a secured creditor was voidable and that case is criticised in one of the commentaries I'll take you to.

If you turn to the next page it’s discussing further an Australian case *Sheahan*. Now *Sheahan* is an Australian case that upheld the disadvantage rule in Australia under their previous legislation and the commentator there just notes, “While the facts of the *Aldridge* case are somewhat unusual, the stricter approach taken has the advantage of simplicity.” And that is true, it is simpler, but my submission is that simplicity was achieved by, improved simplicity and increased scope of voidable transactions was achieved by section 292, and that was a good aim and it was achieved because more transactions became

voidable once the intention test was removed.  But where I depart from the use of simplicity is where it then conflicts with the disadvantage rule because then, in my submission, it’s taking the concept too far.

At paragraph 5.54 the commentator then refers to direct payment contracts, and this is Your Honour Justice Kós in *Ebert Construction* that’s what was dealt with in that case, where there was a tripartite contract where the financier was able to pay the contractor directly and –

**KÓS J:**
That was much more a question about whether the payment was by the company.

**MR CHESTERMAN:**
Yes.

**KÓS J:**
It didn’t really deal with this question at all.

**MR CHESTERMAN:**
Not really but Your Honour in that case did cite the principle in *Allied Concrete* about diminishment of assets.  I believe that was at paragraph 41, and that that statement in *Allied Concrete* is that the underlying purpose of the voidable regime is the protection against the diminishment of assets.  So Your Honour set that up –

**KÓS J:**
Well I don’t think it helps to cite a Court of Appeal decision citing a Supreme Court decision.  It’s the Supreme Court decision that matters.

**MR CHESTERMAN:**
No, Your Honour is perfectly right, I'm just trying to give –

**KÓS J:**
I mean *Ebert* is more relevant I think for this reason Mr Chesterman and that is that it is yet another Court of Appeal decision that upheld the earlier decision in *Levin*. So a difficulty you face is that the *Levin* decision, which is now some 12 years old, has become quite firmly established as a principle, and you have a persuade this court, a higher court than *Levin* and *Ebert*, that the underlying principle is wrong.

**MR CHESTERMAN:**
Yes and when Your Honour cited *Levin* it was as an example of a factual situation where a diminishment of assets was clear, but my submission is that, one of the underlying bases for the submission is the Supreme Court's statement about the underlying purpose being protection against diminishment of assets and my submission is that that is confirming the purpose, the mischief at which the regime addresses and conflicts with a finding in a case that the disadvantage rule does not apply.

The next commentary I'll take Your Honours to is at tab 3. *McPherson and Keay's Law of Company Liquidation* and if we turn onto the first page at paragraph 11-055 and there the author is discussing the basics behind the voidable regime and talking about creditors competing for the company's assets…

**GLAZEBROOK J:**
Sorry, what paragraph are you at?

**MR CHESTERMAN:**
So it's 11-055, page 692 at the bottom, and it says, "It is understandable that the creditors of a company that is in financial difficulties should spare no effort in striving to ensure that their debts are paid in full. However to allow them complete freedom in coming to terms with a company which is facing possible liquidation would inevitably result in a diminution of the fund of assets available for division among other creditors and thus undermine the fundamental rule that the property of the company is to be applied in

satisfaction of its liabilities equally. It has been generally asserted that the consequence of the policy of pari passu distribution is that transactions which affect the disposition of assets or other property before the commencement of winding up and have the effect of reducing the dividend to be paid to the unsecured creditors should be reviewed."

The reason that I have drawn Your Honours to this is because it is a discussion both of the pari passu, the equal treatment principle, and diminishment together. It's no identified that there's any conflict, it's about how they work together and, in my submission, the mischief of the regime, which is first to look at whether there has been diminishment of assets.

The next page that I'll take you to is page 694, it's two pages over, paragraph 11-058, and it's at the bottom of that page. And there the author's talking about the issues that arose from the intention test and, "One of the major problems was that the cases provided that a liquidator could not merely establish that the debtor paid the preference with a view to giving a preference," and it refs to that as, "The onerous task of proving that the debtor's dominant intention in making the payment was to prefer the creditor," and then the author discussed the problems linked with that of putting pressure on the creditors.

**KÓS J:**
I'm just not sure how any of this helps us, Mr Chesterman. These are English authorities, English commentaries, on a different legislative scheme.

**MR CHESTERMAN:**
It's a legislative scheme, Your Honour, from which our scheme is derived, and it is a legislative scheme in which, in my submission, the only difference between the two regimes is that the English regime requires an intention. It might assist if we look at the relevant English provision, which is section 292 of the Insolvency Act 1967, if that would assist, at volume 6, and that is volume 6 tab 20. This is the UK provision, and I'll refer Your Honours to 239(4), and it gives a preference to person if they are a creditor and, "the

company does anything or suffers anything to be done which (in either case) has the effect of putting that person into a position which, in the event of the company going into insolvent liquidation, will be better than the position he would have been in if that thing had not been done." And that is, in my submission, very similar to the formula in New Zealand and it existed well prior to the New Zealand formula because this is a 1986 legislation, and the difference is at subsection (5), which is what keeps the intention test in the UK provision. So my submission is that disadvantage to creditors and intention are two different tests, that in the UK, yes, intention is required, but the UK legislation does not mention the disadvantage principle, the New Zealand legislation has never mentioned the disadvantage principle, and the UK legislation has a formula for preference which is very similar to New Zealand's and was enacted prior to it, and for that reason it is relevant to refer to the UK commentators.

The final part of – I'm back to volume 4 tab3, and I'm now at page 695, and it's headed, "3. Nature of a preference," and the part I'm going to refer you to actually refers to how the legislature treated the test in New Zealand, and it's the last sentence. "It is trite law that the essence of a preference is that a creditor has received more from a company before it goes into liquidation than would have otherwise been received in a liquidation. This concept is encapsulated in s 239(4). The true test of a preference is – does the transaction confer a priority or advantage on a creditor in relation to past indebtedness of the company and is the advantage given at the expense of other creditors who are owed debts at the time of transaction," and then he sets out a quote from Professor Weisberg which confirms that prejudice to the other creditor's point.

The next commentary is at tab 8 and this is Professor Roy Goode's text, *Principles of Corporate Insolvency Law*, and I would note that this text was referred to by a discussion paper in the 2006 reforms, and the relevant part that I'll take you to is the very last page and it's paragraph 13-95, "What does not constitute a preference," and I refer you to the sixth on the list, which is,

"payment to the creditor by a third party which does not involve any call on the company's assets."

**GLAZEBROOK J:**

So explain what that means. Because I can understand it in a subcontractor and contractor, because in fact if there's a clause that says, "Pay it directly to the contractor," the head contractor hasn't any right to that payment and no debt arises in respect of it, so it's actually at a stage where's there's actually no right at all to the asset.

**MR CHESTERMAN:**

Right. Well, what Professor Goode means is that it's an asset of the –

**GLAZEBROOK J:**

Well, what I'm asking you is does he specifically explain what that means in the text that we don't have?

**MR CHESTERMAN:**

Yes. Now I'm sorry, but the further part of the commentary is in bundle 3 –

**GLAZEBROOK J:**

Well, shall we have a look at it?

**MR CHESTERMAN:**

Yes. That's tab 42 and it's the first page in, which is page 581.

**O'REGAN J:**

Sorry, which volume was it again?

**MR CHESTERMAN:**

So volume 3, tab 42, and the passage I'm referring Your Honours to has got the heading, "Improvement in creditor's position must be at expense of other creditors," and it says, "Since s 239 is aimed transactions which disturb the statutory order of distribution, it follows that to be a preference within s 239 the payment or transaction must be one by which the creditor is put in a better

position *at the expense of other creditors.* Accordingly it is not a preference for the company to pay a secured creditor a sum not exceeding the value of the security, for this leaves the position of other creditors unaffected. By the same token, a payment or transfer is not a preference if made to the creditor by a third party, except to the extent to which the ultimate burden falls on the company's assets that would otherwise have been available to all of its creditors, as where the third party is entitled to recoupment from the company and that right is secured," and then he refers to the decision of, a difficult decision of the Australian High Court of *G & M Aldridge Pty Limited v Walsh,* and that's the criticism of that authority that I referred to. If you'll just give me one moment.

If we turn to the next page, 582, and I'm about midway down, on the left you'll see of section 239 of the Insolvency Act 1986 and above it the author is discussing the Australian authority *Sheahan* which upheld the disadvantage rule in the context of the *Aldridge* decision and then the author says, "If a third party chooses to pay a particular creditor without this resulting in any diminution in the company's assets, the creditor's position is undoubtedly improved but the payment is not within the mischief at which the preference provisions are aimed. There would be no doubt about that if the third party made the payment direct to the creditor without involving the company. Why should it make any difference if the payment comes from a fund held by the company but impressed with a trust or charge in favour of the third party to secure an amount exceeding the value of the fund? Assuming that the burden of the payment does not ultimately fall on the company's assets, the payment is not in any real sense made by the company at all; it is merely the vehicle for the transmission of the third party's funds. Again, the mere fact that the payment is made at the company's request or that it is a party to the transaction under which the payment is made by another does not by itself engage the company's assets so as to give rise to a preference."

So there the author is talking about introducing that concept of payments by the company and the fact that they do not automatically amount to a

diminution of assets. There is a case that I wish to take Your Honours to which is a Canadian authority and it is in bundle 2 at tab 24.

**KÓS J:**

Assuming that these are parties who know what they're doing, the third party is being used in these examples to effectively marshal creditors to prefer the interests of the paid out creditor over that of the incoming creditor who then faces insolvency. Isn't that a device, assuming knowledge on the part of all parties, isn't that a device that will simply allow exactly the mischief that section 292 is aimed against, and that is preferring of a creditor by the introduction effectively of a sacrificial creditor, and that sacrificial creditor, assuming knowledge, is almost certainly going to be part of an associated group.

**MR CHESTERMAN:**

Well Your Honour if the sole mischief at which the section was addressed was just preference of one creditor doing better than another, then I would agree with Your Honour. But the reason I disagree is because I say that the section is not targeted at just that. It is, at its very core, protection against diminishment of assets. So if a third party comes in, that replacing, swapping out unsecured debts, that doesn't affect the situation in terms of the underlying reason for this regime. But if the regime as Your Honour says is merely, as the current law says it is, then that's right. Now there are two cases, and I –

**KÓS J:**

We need to grapple with why that's wrong, why that's the wrong policy for this Court to embrace. I mean history isn't enough here. There's been legislative reform.

**MR CHESTERMAN:**

Yes, can I take Your Honour to the one case on this, so the area of it I've been addressing is my third submission, I've been addressing how pari passu equal treatment and disadvantage have been addressed together in the UK

and why they don't conflict, why disadvantage is the precursor for any voidable transaction in my submission. There's one case I'd take you to from Canada and then I will take you to their legislative development of section 292.

The case from Canada is *Re Urbancorp Cumberland 2 GP Inc* 2017 ONSC 7156, 54 CBR (6th) 311, and it is volume 2 at page 24, and what occurred in that case was that money was – it's volume 2 at tab 24.

**O'REGAN J:**
This is a first instance case is it or is it a…

**MR CHESTERMAN:**
Yes it is Your Honour. It's the highest trial court. The paragraph I wish to take you to, so what occurred here was a payment of tax through borrowing funds that was paid to the creditor and at paragraph 32 the Judge notes, "Edge's payment to the CRA was economically neutral to Edge. It replaced one liability owing to one creditor with the exact same liability owing to another."

I'm sorry, it's page 5 of the judgment, I'm reading from paragraph 32, which is about half way down, and it's talking basically about that unsecured creditor swap that I mentioned at the start. "The recovery of unsecured creditors was not prejudiced by $1 by the interpretation-company loan of funds into Edge and the subsequent payment to the Contractual Remedies Act."

Paragraph 33, "At its most basic conceptualization, '[a] preference occurs when an insolvent debtor pays one or more creditors ***at the expense of other creditors***.'" And I ask Your Honours to keep in mind that word "expense" because expense, in my submission, means disadvantage at their cost that they have suffered, that there is less available for them, and that is a word that will come through in the next phase of the argument about the legislative reform.

**GLAZEBROOK J:**

What had happened in this case, the group company had lent money that actually sounds as though it did go into the money but with the express purpose that it had to be used to pay the tax, is that right?

**MR CHESTERMAN:**

Let me just have a look at my summary Your Honour. Yes, so the money went into the company solicitors, I understand.

**GLAZEBROOK J:**

But it was specifically, as I understood it, it was a loan with a specific tag that it be used to pay tax?

**MR CHESTERMAN:**

Yes, and my submission is it’s similar – well my submission is that the MSH2 payment is even a stronger example of this type of fact. There was no need for a specific tag to be attached, earmarking is the principle that’s been referred to in the United States, and comes up from time to time, and all that is, in my submission, is a reflection of that principle. Does it diminish the assets of the company available to the creditors? The earmarking principles says well if it’s earmarked for a specific purpose it’s not available for the general pool of creditors, and so that is that tag that Your Honour is referring to in this case –

**GLAZEBROOK J:**

Well that can't really be right, can it, because you can earmark as much as you like, i.e. earmark that this is only to be paid to make my furniture that I want to be made, I've earmarked it quite clearly, but that doesn’t mean if they go into liquidation or insolvency before my furniture comes to me, that I'm not in the general body of creditors, does it?

**MR CHESTERMAN:**

Well I'm not arguing the earmarking rule here Your Honour I'm just – in fact I haven't looked into the earmarking rule, it’s been mentioned a couple of times

recently in seminars, but I'm just mentioning as perhaps an example of the application of the rule that the assets must be the company's and available for its general body of creditors, and in this case it was found that the assets weren't and that it had zero impact on the company's balance sheet.

**KÓS J:**
This simply seems to be the exemplary. It doesn't really grapple, Mr Chesterman, with the question I put to you which is, what is wrong with the policy that's expressed in *Levin* and then in the Court of Appeal below. What's the problem?

**MR CHESTERMAN:**
The problem with the policy Your Honour is that it puts the, it creates this wrong situation of money coming into the pool of creditors that never would have been available for them in the first place. If you look at this case, for example, if this case was made voidable then it's imposing upon the third party a separate legal entity free to do with their money what they wish, subject to contractual obligations, it forces upon them a requirement that regardless if they're only going to pay it to the creditor that that means they're going to pay it to the company.

**GLAZEBROOK J:**
But you accept there's a debt to them to pay it to the company, the debt arises, don't you accept that?

**MR CHESTERMAN:**
Excuse me, Your Honour, I…

**GLAZEBROOK J:**
I mean – oh, well, I think I see what you mean, sorry. It was a different point.

**MR CHESTERMAN:**
Okay. So I suppose that answers it briefly, Your Honour.

**KÓS J:**

Well, I don’t yet. So if you want to run that again please?

**MR CHESTERMAN:**

Yes. So –

**GLAZEBROOK J:**

I think it’s because it doesn’t go into the company and they chose for it not to go in the company I think in the point.

**MR CHESTERMAN:**

If the money was never part of the company’s pool of assets that it could have drawn on to pay its creditors, it was never available for them. So if the Court reverses transactions, where those assets were never available for the creditors then it’s putting them in a better position than they were before the transaction. The purpose of these provisions is to reverse the transaction, to restore the creditors to the position they were in before the transactions occurs. But that’s not what happens in these cases. The transactions is not reversed, the money doesn’t go back to the third party, the creditors are not put into the position they were in before the transactions, they’re put into a better position because money is brought into the pool that the third party would never have paid to them in the first place, and to presume that the third party would have paid it into the creditors’ pool is to introduce, in my submission, an evidential presumption and to interfere with the rights of the third party over their own money.

**KÓS J:**

But isn’t that...

**O’REGAN J:**

But isn’t the regime trying to stop preferential payments, full stop? So if we interpret the section the way that it was interpreted in the *Market Square* case, payments such as this one to Robert Jones would never have been made.

The objective of ensuring all creditors being treated equally will be achieved, won’t it?

**MR CHESTERMAN:**
Well, once against, Your Honour, I do not agree that the – I agree that by reading the section literally and a plain-meaning approach, that the interpretation is that the section is solely focused on whether one creditor does better, that is the plain-meaning approach. What I am advocating and what I submit is the right approach is a purposive approach to that section.

**O’REGAN J:**
But there’s nothing in the section that indicates that's the purpose.

**MR CHESTERMAN:**
But, Your Honour, that has always been the purpose, and it’s stated in paragraph 1 of *Allied Concrete.*

**O’REGAN J:**
Well, it was the purpose of the old law, but this is a new law.

**MR CHESTERMAN:**
But *Allied Concrete* was just a case decided out of the Supreme Court two years ago. The opening passages, the underlying purpose of the voidables regime is protection of creditors against the diminishment of assets of the company available to them, that’s paragraph 1.

**O’REGAN J:**
Yes, but that is achieved by having a hard and fast rule that nobody can be preferred.

**MR CHESTERMAN:**
But that rule does not achieve it, because in the example I –

**O'REGAN J:**

Yes, it does, it does achieve it, because it stops people avoiding the section 292 regime by getting payments made out of a third party, it's exactly what this case shows. If the parties had adopted a process that made it clear that Robt. Jones wasn't going to get any advantage by being paid by a third party the payment wouldn't have been made and therefore Robt. Jones and everyone else would have been treated in a pari passu way, which is the underlying regime of our insolvency law, that all creditors are equal.

**MR CHESTERMAN:**

Well, my submission, Your Honour, is that where there is a scenario where the creditors are put in a better position by assets being paid to them which never would have been available in the first place that the section is going well beyond the purpose of the regime, it's going well beyond the mischief that the regime was designed for. It was never the purpose of the regime to increase the pool of assets.

**O'REGAN J:**

But, I mean, you're just arguing, you're saying the purpose of the regime was this therefore the that's what the section says. All you're doing is it's a completely circular argument.

**MR CHESTERMAN:**

But I –

**O'REGAN J:**

If we don't accept that that's the purpose that's the end of your argument.

**MR CHESTERMAN:**

That's right, Your Honour, and I –

**O'REGAN J:**

If we say the purpose of the regime is to make sure nobody's preferred, isn't that the end of your argument? And that seems to be what section 292

specifically says. So why should we interpret in a way that means something different from that?

**MR CHESTERMAN:**
Well, if I may move on to my next submission, Your Honour –

**GLAZEBROOK J:**
Well, perhaps we take the adjournment at this point. Is that a convenient time, Mr Chesterman?

**MR CHESTERMAN:**
That's fine, thank you.

**COURT ADJOURNS: 11.35 AM**

**COURT ADJOURNS: 11.51 AM**

**MR CHESTERMAN:**
May it please Your Honours. So I was just finishing off on the *Urbancorp Cumberland* case and the remaining paragraphs 34 and 35 – that was at bundle 2, tab 25, page 5 – just said that, although the creditor may have been referred in the vernacular, the general creditors were not disadvantaged and therefore the transaction did not impact with the mischief on which the provisions were aimed and that had those creditors understood that the loan was about to be made they had no added incentive to bankrupt Edge, "They would suffer no prejudice that might lead them to race to judgment or otherwise to lose faith in the fairness of the bankruptcy system. Nor would the overall pot of assets or their respective shares of Edge's assets be diminished. Put simply, while the payment might have preferred the CRA in the vernacular and one might question the corporate appropriateness of the overall transaction whose purpose seems to have been to protect the shareholder rather than the companies, the transactions caused no prejudice to creditors and caused none of the mischief that preference regulation is designed to prevent."

I'll now continue on with I was being asked about, well, that may have been – I hope I'm re-stating this correctly – under the previous provision it may have been a requirement to disadvantage, the disadvantage may have applied but that's old news and it doesn't apply any more, and that that was dealt with by *Levin*. My response is that *Levin*, when you look at that decision it doesn't address at all *Lewis v Hyde*, it doesn't go through any of the legislative material behind the enactment of section 292. It doesn't even mention the fact that in fact disadvantage had never been mentioned in New Zealand's legislative in any provision nor was it mentioned in the UK but it applied.

So what I'm going to take you to now are some of the Parliamentary materials and that will be in support of my submission that when there is a fundamental common law principle, particularly when it's fundamental, the Court will be loath to find that it has been extinguished by new legislation, and in particular in New Zealand a recent case out of the Supreme Court which was *Kumar* in which section 7 of the Contractual Remedies Act 1979 was addressed stated as a code but even so common law principles were imputed to it.

The first document is at bundle 3, tab 28, and this is the Australian Law Reform Commission report. This is the document on which the New Zealand Law Commission report number 9 drew from in relation to the liquidation provisions. And the part I wish to refer you to is the very first paragraph, 68 – this is under chapter 14, "Avoidance of antecedent transactions," and it says, "Existing legislation provides three main ways of reviewing and avoiding transactions which were made before the commencement of a formal insolvency administration and which have reduced the pool of property available for distribution to creditors." My submission is that right at the forefront of this report the Commission is putting in place what this voidance regime is targeted at and an underlying principle, and if we turn next to the next page at paragraph 630 the Commission states that, "The broad policy evident in the existing legislative framework for dealing with the type of antecedent transactions under consideration should continue."

So this is just two paragraphs later from their reference to protecting against the reduction of the pool of assets and this paragraph confirms that the basic policy is to continue. And on the next page at paragraph 632 it sets out the Commission's decision. They heard submission on whether or not the current policy should continue and they decided that it should continue and if there was a change, as one was suggested, it would undermine two fundamental principles in insolvency law and it refers to equal sharing between creditors and promoting an orderly process during formal insolvency. But what's interesting about this is it has right at the start of defining a voidable transaction defined it in terms of the common law that has been around since Lord Mansfield's cases, and there is nothing in this document which indicates that there was any intention by the Australian Law Commission to remove that underlying requirement. And the next paragraph is 638, and there the Commission –

**GLAZEBROOK J:**
Isn't the submission at the beginning that the whole of the insolvency regime is reducing the pool of creditors and then one alternative submission is just looking at one particular part and that was narrowing the preference regime right down, which has been rejected for the reasons given in that paragraph which had nothing to do with diminution of assets?

**MR CHESTERMAN:**
That paragraph is referring specifically to some suggestions about an alternative way to –

**GLAZEBROOK J:**
Well, that was narrowing the preference regime down.

**MR CHESTERMAN:**
It was narrowing it, right. But when the answer comes through it is that the underlying policy, basically what a preference is, remains, and at the very first paragraph of this chapter on voidable preferences the definition includes transactions which have reduced the pool of property available for distribution.

I cannot find anything in the report subsequently which in any way targets the removal of that requirement and, as I'll show you, in terms of the law my submission would be that as this was an underlying principle of voidable transaction law if it was to be removed by Parliament you would at least expect it to be mentions, but it isn't, and it's not mentioned in the New Zealand section either.

The other relevant part is paragraph 638 where the Commission sets out how it proposes to define a voidable transaction, and it essentially sets out the formula which was utilised in section 292. But we must recall also it's pretty much the same formula that's in section 239 of the UK Insolvency Act, which was 1986. So the formula it proposes there, and keeping in mind that there was a decision not to change, there is nothing evident here that they were going to change what the nature of the preference was, it doesn't include the reference to expense to creditors or disadvantage, and that's not unusual because it's never been mentioned, it is just as was said in Privy Council *Lewis v Hyde*, it's an underlying common sense fundamental principle that has always been there.

**O'REGAN J:**
It's pretty remarkable though, isn't it, that something as fundamental as you say it is, is routinely left out of every statute. Why? I mean why would Parliament do that?

**MR CHESTERMAN:**
I can't –

**O'REGAN J:**
I mean I can't think of any other example where a fundamental principle of a statute is deliberately or inadvertently not mentioned anywhere in the statute.

**MR CHESTERMAN:**
I suppose, as you'll know, one of the big focuses of this reform was simplification and in terms of liquidation, as I'll take you to, there were really

two, there were three things that happened. One was they reduced liquidation procedures from five down to one, so there's only one type of liquidation procedure. The other simplification was reduced court involvement so that liquidators don't have to keep going off to court all the time, and the next simplification was in the wording used so that the Acts, as a restatement, could be a document of first recourse for your everyday company, and keeping in mind that in New Zealand over 70% of companies have no employees and I believe over 90% have five or less, so that was an aim, and that, I'm speculating Your Honour but that might explain it. It might also be that it was never mentioned in the section before. It might also be, as stated in *Lewis v Hyde* by the Privy Council, that it's so basic and fundamental that why would you attack a transaction that hasn't diminished the assets. But beyond, that's the only answer I can offer on that Your Honour. But I suppose where it –

**KÓS J:**

Isn't your third point, that is to say that the Act is a document of first recourse for business people.

**MR CHESTERMAN:**

Yes.

**KÓS J:**

Isn't that a point really heavily against you because the ordinary business person, looking at that provision, would not see that the disadvantage requirement would proceed in ignorance.

**MR CHESTERMAN:**

I would accept that that would, that's right Your Honour, and that would be, in my submission, a fault with the legislation, but no legislation is perfect and I'm not going to take you through all of the debates in this case but you have them in volume 5 and what is apparent is it was a six year gestation process for the 1993 Act through numerous, well there were numerous law reform reports and when Parliament comes to asses it, particularly in the second and

third reading, they say, you know, this is a really complex legislation. It was a reform of the entire Companies Act for the first time in a very long time, so they have these goals, or objectives of simplification and restatement, but they weren't achieved in all cases and for example directors' duties, there initially was an issue about are these a codification and I think the position is they are not a code of directors' duties and there are other areas of the Act, and once I finish going through these materials I'll take you to an excerpt from Carter on statute interpretation which specifically refers to the Companies Act and said that it is, it's really a partial code and it's littered with examples of fundamental principles that haven't been stated, and that simply by reading it, divorced from the common law, a common person would not, a non-lawyer, a lay person, would not be able to understand exactly what it is meant to convey. But regardless, where that comes back to, Your Honour, is we can't do anything about that but what we can look at is the legislature's intention and what the law is, is that if the legislature is going to remove a fundamental principle it will say so and the Court should be very slow to assume that Parliament intended to do something like this, that it never stated it intended to do.

The next document I'll take you to is the New Zealand Law Commission report number 9, which was June 1989, and this is six months after the Australian Law Commission report, and it is at bundle 3, tab 28. Sorry, that's the wrong reference Your Honour, tab 37. I haven't provided Your Honours the entire report but I would encourage you to read it particularly in relation to the liquidation because it does address all of those areas of simplification and harmonisation and what's apparent in it is that nowhere does it state in relation to voidable transaction that they are to be a code, that everything has been confined and sorted out, simply those aims for simplification were sought. So at page 30, which is the first page, it says there at paragraph 121, "We are required to have regard to the desirability of simplifying the expression and content of the law, as far as that is practicable." So that was a desire of the legislature, but it does not, in my submission, made the Act a code.

If we turn to page 151, sorry 150 and 151, they're on the same page, this is Part 14 where it address liquidation and these are where the concept of simplification came through that I mentioned. At 640 it talks about five ways to end a company, and then that's going to be reduced to the two options it refers to at paragraph 641, and then at 642 confirms simplification in relation to liquidation and refers to the liquidator having to refer matters to the Court frequently. So at 644 it refers to that reduced role of the Court.

On the next page, at paragraph 645, it looks at the second major simplification, I'm sorry the second major simplification was talking about the reduced role of the Court. 646 is where we start getting near to the voidable discussion, and it talks about innovations, and my submission is this reference to innovations is crucial for the Court's understanding of what Parliament intended because when it's talking about innovations it's saying to the reader, these are new aspects, things that have changed, and it first there discusses the prohibition against monopoly suppliers. 647, they talk about an assetless company fund. 648, enforcement of liquidator's duties, and it says here at 649, which is the relevant paragraph, "The final innovation is that voidable transactions are dealt with differently. The focus at present, when a creditor receives payment in preference to others, is on the intention of the debtor company. This means that in circumstances where a creditor is preferred through no voluntary action by the debtor, for example, where a creditor is able to coerce the debtor, the transaction cannot be attacked. This leads to the unsatisfactory situation where creditors may be treated differently according to the quirks of their circumstances. The purpose of a voidable transactions regime is to avoid this, yet the present law permits it. Our proposals, which are drawn from both the Australian Law Reform Commission's Report…"

So in my submission what 649 is about, is it's putting into focus what the change is. The change is the removal of the intention requirement, and I know Your Honour Justice Glazebrook took a different view on that, that that meant throwing out, I suppose, the baby with the bathwater, disadvantage as well, but my position on that is disadvantage is a separate concept. It was, in

my submission, mentioned at the first paragraph of the Australian report, and it has not been ousted in any way by the words of this Law Commission report.

The next paragraph relating to voidables is at paragraph 696, which is page 162, and it refers to the draft provisions which were at sections 225 to 228 and I've provided a copy of those in the additional volume, and the paragraph about effect of the transfer that has been used subsequently comes from this paragraph 696, and it's near the bottom of the paragraph, "As can be seen, the emphasis is on the effect of the transfer. Any system which creates a regime rendering some transactions void has to choose between competing interests." So all that merely does is confirm this focus on effect, and my submission is that it is not absolutely clear from that that Parliament meant to exclude the disadvantage rule, in fact to the contrary disadvantage is one of the underlying requisite effects of the voidable transaction when you look at the history of the voidables regime.

I do apologise for this. If you can leave bundle 3 out and take bundle 7, these are just a further few pages from the same report. And at bundle 7 can I ask you to turn to page 204, "Policies for Company Law," and it's paragraph 20, third bullet down, and this is that, "provide better accessibility to company law by setting up the Act as the statement of first recourse in identifying rights and duties within the company." So that was the stated aim, that was the desire. But, as is evident from the analysis in Carter, it was not achieved completely, although it was, certainly did a great deal to improve accessibility and simplicity, and I suppose that is one aspect of the Act, it did achieve aims in many different ways. Unfortunately it didn't consider the need to state the advantage rule. The next relevant part of this is at –

**GLAZEBROOK J:**

Can I just check how we're going in terms of your points you wanted to make, because you really will have to finish by lunchtime. So I'm not sure that just going through this in excruciating detail is going to help your submission. Your submission is there's nothing in this material –

**MR CHESTERMAN:**
Yes.

**GLAZEBROOK J:**
– that suggests that they were wanting to do away with the disadvantage rule.

**MR CHESTERMAN:**
It is, Your Honour.

**GLAZEBROOK J:**
So are there really particular things that might show that that was the case, that they even had it in mind or didn't have it in mind?

**MR CHESTERMAN:**
So Your Honour's suggestion is very helpful, thank you.

**GLAZEBROOK J:**
It's just I want to make sure that you get through all of your submissions rather than being tied up taking us through material is just making a point.

**MR CHESTERMAN:**
Well, let me – I'll finish with the report number 9 here, but let me just summarise a couple of, one further aspect of it, which is at this volume at pages 11 and 73. It's about the harmonisation with Australian law. Now one of the desires also was to not to conflict with Australian law and to allow for harmonisation because of the trading relationships between the countries. But at the date of this report Australian law was in a state of disarray, they hadn't enacted any new legislation or draft legislation, and the Commission said it was not an acceptable model to follow. The Commission also accepted that there will be differences between the two laws. And so the point of my raising that is that what we had was, the Commission is simply saying, "We are drawing from the Law Commission's report number 45 from 1988," which I've taken you to. But what they are not saying is, "We should follow

Australia’s law or follow their legislation or how they’ve drafted it,” because indeed that legislation didn’t exist at this time.

At bundle 3 tab 29, which is the Companies Bill Explanatory Note, I’ll just take you to one page of that, which is ix, Part XIV, Liquidations, item (d), and the explanatory note says, “Reform of the law relating to voidable preferences in that attention is directed not to what the debtor company intended but to the effect of the transaction and whether it was made in the ordinary course of –

**GLAZEBROOK J:**

Sorry, I’m not quite sure where you are.

**MR CHESTERMAN:**

So I’m at volume 3, tab 29, and the Companies Bill Explanatory Note at the top, I’m on the right side of the page, page ix, under Part XIV, Liquidations, and it says, “The significant reforms in this Part of the Bill are,” and at (d) it describes what those reforms were in relations to voidable preferences.

I will not take you to the parliamentary debate so provided them in bundle 5 and indexed them. But there’s really just one crucial passage, which is at bundle 5, tab 5, it’s the second reading of the Bill and that just draws attention to the very same reform that has been discussed so far that, “We’ll not focus on the intention but on the effect,” the words are almost identical. So that is the thrust that comes through all of these documents, “We’re not focusing on the intention any more but the effect."

The final document is at bundle 7, it’s a document referred to in *Allied Concrete* at paragraph 42 and it’s a Ministry of Economic Development Tier One Discussion Document. It’s at page 243 of bundle 7 and we’re at page 54 of the Tier One Document. And the reason this is referred to in *Allied Concrete* is because it was part of the reforms in 2006 where the ordinary course of business law was replaced and it talks – I’m about halfway down, beginning, “The second category.” “The second category of provision is designed to set aside those transactions that diminish the value of the

debtor's net assets in a certain period before formal insolvency." So what they're talking about there are antecedent transactions. So as late as the date of, as this paper, 2001, which was after the 1993 reforms, this refers to the nature of avoidable as –

**O'REGAN J:**

Yes, but as we discussed at the beginning, every transactions reduces the debtor's net assets, so that's just patent nonsense isn't it?

**MR CHESTERMAN:**

Well, my submission is that by referring to that principle they're referring to the –

**GLAZEBROOK J:**

But isn't the voidable preference regime done at the first one, not the second category? So this was talking about gifts and improvements and stuff. So in fact the first paragraph doesn't refer to diminishing value and the second one does, specifically. So the first one it says it's pari passu and that's the aim…

**MR CHESTERMAN:**

Well, the first – Your Honour, if you're at the first one, if you look at the last sentence, it talks about inequitable for a debtor to pay one creditor in full on the eve of liquidation at the expense of the general pool of creditors.

**GLAZEBROOK J:**

Well, that's because they get a preference over them.

**MR CHESTERMAN:**

Well my submission is that "expense" is a word that has been used throughout –

**GLAZEBROOK J:**

Okay, I understand the submission.

**MR CHESTERMAN:**

I won't take you to any further material. I'll take you to Carter on statutory interpretation which is also at bundle 7, and the relevant part starts at page 180. This part of Carter refers to encroachment of statutes on areas of common law so I suppose in other words where situations where statutes might oust the common law. At page 181, the next page, Carter defines what a code is, and it's one that, "Expressly abolishes the common law in a particular area and replaces it with a set of statutory rules." My submission that hasn't occurred here. This is not like one of the other New Zealand statutes which clearly expresses the statute to be a code.

The next page is 184 and here Carter refers to a stated code, section 7 of the Contractual Remedies Act 1979, declared to be a code and then refers to the case of *Kumar v Station Properties Ltd* which found that a part of the common law still applied, even though it was stated as a code. The next page is at 189, and this is about partial codes. The last paragraph on the page it says, " At other times, however, this retention of the common law is not so explicit. The Companies Act 1993, containing nearly 500 detailed sections, might appear to be a complete statutory code on the subject of company law. However, it takes much for granted, and does not deal with some of the fundamental concepts of company law. The Act has to be read against the background of many decisions. No one reading the Act by itself could gain a proper understanding of the subject."

The next page is 193 and I'm at the third paragraph and it says, "The more fundamental the common law principle, the more concerned the court will be to hold the statute has not excluded it. If it expresses a fundamental long-standing principle of justice the court will be ready to retain as much of it as possible by strict construction and by "reading down'' the statutory provision. Thus, the statute giving power to grant search warrants…" et cetera. That is the point that –

**GLAZEBROOK J:**

The long-standing principle of justice is really a sort of common law Bill of Rights isn't it, that the Courts will be reluctant to think that Parliament meant to overturn it, but that's a totally different concept from what you're saying now.

**MR CHESTERMAN:**

I believe it's a, it rises to a legal presumption that when there's a fundamental common law principle that it is, it can't be extinguished –

**GLAZEBROOK J:**

But when they're talking about fundamental common law principles they're talking about the fundamental common law Bill of Rights in this context, not a principle of common law related to a particular subject that may or may not have been dubbed fundamental in case law. So if it's expropriation of property for instance, or it's locking people up without a warrant or cause or bowling in and searching, all of those things are the fundamental principles of the common law that's been spoken about here. The right to be heard, that type of …

**MR CHESTERMAN:**

Well my submission is that this principle of disadvantage is as fundamental as any other major principle in any other area of law. It allows a legitimate transaction to be reversed when the creditor had, on the face of it, entitlement to keep the money. There's nothing minor about the power to reverse a transaction and it has been a principle that has been around from the inception of the regime. So I accept Your Honour's point that many of these cases do relate to those Bill of Rights type situations, but it's not necessarily always the case. I've provided Your Honours with the Laws of New Zealand excerpt on this topic and in the footnotes it goes through many different cases and one of those was the, it was the case of Sir Ian Barker's, the Trademark Act, and when that was enacted whether it codified and did it remove a common law principle that ownership of a trademark was gained by use and the Court held that it didn't exclude that principle. So there are a number of

different types of cases where a fundamental principle is held to continue to apply unless it's excluded in my submission.

The next page is 199, sorry, if we just go back, 195, and there Carter refers to a Court of Appeal decision in *Grant v Lotus Gardens Ltd* [2013] NZHC 1135 where it held that the setting aside procedure in the Companies Act, 294 to 296, "Is not a code excluding other common law or equitable rights and remedies by which a liquidator might try to attack a preferential transaction." There it's talking in the context of breach of director's duties and indeed in, I've provided a case to Your Honours of Justice Heath's, as he then was, *Benton v Priore* [2003] 1 NZLR 564 (HC) where His Honour found that the part 16 of the Act, which is the liquidation section, is not a code in respect of directors' duties related claims.

The concluding paragraph I provided I suppose sums up the position of Carter at 198 that there are no straightforward answers. "Everything depends on the construction of the Act in question, the ability of the common law and statutory provisions to 'live together' without too much difficulty, and how fundamental the common law principle is." So that's at page 580 and 581.

I've now completed the material relating to the legislative machine behind the enactment of section 292 and I've now arrived at my argument for why the Court's findings in *Levin* were wrong. I've already taken Your Honours to the wording of section 292, and my submission on that is that that wording does not exclude the disadvantage rule. The second point is that it's also my submission that there was no intention by the legislature to exclude the rule and *Levin*, although the leading authority in this area, does not address the legislative history and it does not address *Lewis v Hyde*. It very briefly states that the principle does not apply because it's ousted by the plain meaning and wording of the legislation.

May I just ask what time the break for lunch is, just so I can time myself?

**GLAZEBROOK J:**

One o'clock.

**KÓS J:**

I do want you to come back, at least for my part Mr Chesterman, to this question of whether there was an actual diminution of assets and the position of MSH2. I know you're getting there but please don't forget to take us in time to that point.

**MR CHESTERMAN:**

Yes so –

**GLAZEBROOK J:**

I think MSH2 didn't, wasn't able to prove in the liquidation, was that in your submissions?

**MR CHESTERMAN:**

That's right.

**GLAZEBROOK J:**

And why was that the case? I don't think you explained that?

**MR CHESTERMAN:**

The evidence – we were unaware of that until trial – that was in the evidence of one of the experts for the liquidator, so we don't have much information behind it. But it appears that the liquidators held that there was a set-off of money they were owed by MSH2. Because what occurred was MSH2 went into administration in Australia and the directors said that MSH2 owned all the licences and Northern Crest claimed that it owned the licences and made a huge claim in the liquidation and the administrators declined the claim, they accepted it for $1, and they said, "There is no value in these licences whatsoever, we don't know what you're talking about." So that's the situation and I believe that's the underlying reasoning for why the liquidators in this case declined MSH2's application to be a creditor.

The *Levin* case is at bundle 2, tab 17, the relevant paragraphs begin at 38 and are concluded by 42. So at 38 they address the topic about diminishment and Their Honours refer to *Chatfield v Mercury Energy* and *Cobb & Co Restaurants Ltd v Thompson* (2004) 9 NZCLC 263,645 (HC), and in the former, *Chatfield,* they refer to Justice Randerson's statement that the focus of section 292 is very different from its predecessor, section 309, it's not concerned with the effect of the transaction on the net assets of the company. Now *Chatfield* – I suppose because this is such of a crucial part of the argument I will take you to the case. That is at bundle 1, tab 7…

**O'REGAN J:**

I honestly don't think you need to. I mean, we've read all this material.

**MR CHESTERMAN:**

Alright. Well, I –

**O'REGAN J:**

We know what *Levin* says and we know what it overruled. What's wrong with it? That's what you've got to tell us. What error was made in *Levin* and what error was made by the Court of Appeal in this case?

**MR CHESTERMAN:**

Right. The error in *Levin*, Your Honour, was the same error that was made by the Court of Appeal in this case, which is that it did not consider the legislative history of the section and did not even look at – well, apparent on its face – report number 9, the Australian Law Commission report, the debates, it simply looked at section 292 on its own, essentially, although it did not say a code, as a code.

**O'REGAN J:**

It's not unorthodox in statutory interpretation cases to start with the words and then look at the purpose and then come up with an answer.

**MR CHESTERMAN:**
Of course.

**O'REGAN J:**
So it's hard to say it's a mistake not to look at an Australian Law Reform proposal of 20-something years ago as a starting point, why is that a mistake? That's a completely orthodox way of interpreting a statute.

**MR CHESTERMAN:**
Your Honour, I'm not saying it's a mistake to look at a section, it's exactly what I did at the start of my submissions, I took Your Honours to the section, that is the starting point of course. But when a fundamental principle such as this which has been around for this long is apparently by an interpretation of the section no longer there, then it is my submission that a purposive approach is required and the Court does need to look at has that common law rule been extinguished, is this a code or is it not?

**O'REGAN J:**
I disagree.

**GLAZEBROOK J:**
Well, perhaps the best way is to say nothing to do – I don't find that very helpful. The best thing is to say, well, what is a purposive interpretation of 292 and what do you say to that? Is it anything more than the legislature didn't specifically overrule a principle that's been there for a long time and which has been described as fundamental?

**MR CHESTERMAN:**
*Levin* was wrong because they failed to confirm that the principle disadvantage continued to exist and had not been ousted by Parliament or its drafting of section 292, and they were wrong for the same reasons that I have elaborated on earlier in relation –

**GLAZEBROOK J:**

Well, that's what I said, does it come down to –

**O'REGAN J:**

So why are we dealing with this? You're just going over the same ground, *Levin's* wrong for the same reason that this case is wrong. So why do we need to focus on *Levin*?

**MR CHESTERMAN:**

Well, Your Honour, it is the most important case and it is wrong for the same reasons, but I thought it might be helpful to the Court if I looked at the reasoning of this Court and that might assist with my submission that it was an error, and my purpose is simply to show you the cases it relied upon and show the very brief analysis that applied and to show you why the cases that it relied upon were wrong, and the first case it relied upon was *Chatfield.* That did not deal with diminishment of assets at all, that was an ordinary course of –

**GLAZEBROOK J:**

Well, perhaps you can just explain to me what the policy reason is for the distinction between paying via an overdraft, having a third person pay or borrowing and then lending on and then paying? What's the policy reason for your distinction?

**MR CHESTERMAN:**

The policy reason or the distinction between these hypotheticals is diminishment of assets because the –

**GLAZEBROOK J:**

No, no, that doesn't answer anything. What's the policy reason or saying if I say to the third party, "Instead of paying me pay a creditor," or if I say to the third party, "Pay me and I'll pay the creditor," what's the policy reason for the distinction between those two circumstances?

**MR CHESTERMAN:**
I'm not sure I understand your question, Your Honour, because the only answer I am able to provide is that –

**GLAZEBROOK J:**
Well, you say there's a difference between those two situations.

**MR CHESTERMAN:**
There is.

**GLAZEBROOK J:**
What's the policy reason for there being a difference between those two situations?

**MR CHESTERMAN:**
One diminishes the total assets of the company available to creditors and one doesn't.

**GLAZEBROOK J:**
And why do you say that's the case and why would you make a distinction in that circumstance just because of the way the transaction happened, and in some cases how do you even know that's the way the transaction happened?

**MR CHESTERMAN:**
Your Honour, my submission is simple. It is that the disadvantage rule applies and when total assets of the company available to creditors are diminished that is a voidable transaction, and when they're not diminished it's not. Now there can be many hypothetical situations that are raised but it's not really, they don't affect the requirement of this principle, Your Honour. The principle was in place, it was either removed by Parliament or it wasn't. So in my submission it's irrelevant whether or not in some hypotheticals it becomes confusing or not. The argument today is that the principle existed, which is clear from *Lewis v Hyde,* that Parliament never removed it, which I say is clear by looking at the debates and the reports on which they relied,

and that when section 292 as drafted does not explicitly remove it either and it's not a code, and that's the straightforward argument, and I cannot convince Your Honour any further on any further policy reason because I believe the mischief and the policy behind the voidable provisions –

**GLAZEBROOK J:**
So you're saying even if there's no policy reason for it and it's a totally idiotic rule we should, under the new regime, still retain it because it is a fundamental principle which was not mentioned at all in any of either the previous legislation or this legislation and this legislation takes a totally different approach from the previous legislation?

**MR CHESTERMAN:**
I'm not saying that at all, Your Honour, I'm –

**GLAZEBROOK J:**
Well, I think, you are, aren't you?

**MR CHESTERMAN:**
Well, first of all I'm saying –

**GLAZEBROOK J:**
So if we think there was no policy reason for the distinction in the first place why should we retain it when – and you can't explain a policy reason either for the difference between those two situations? Your answer to me was, well, it's just against the diminishment rule.

**MR CHESTERMAN:**
Which is the mischief at which the entire regime is targeted, diminishment of assets. There is no stated policy of Parliament to remove that –

**GLAZEBROOK J:**
Well, what that says, it's actually looking at the pari passu and under this somebody gets more than they would have done under a liquidation because

they wouldn't have if the liquidation that happened have got the 260,000 they did.

**MR CHESTERMAN:**

My submission is a pure application of the pari passu rule leads to the absurdity of the situations we've looked at where a third party pays money to a creditor directly and the liquidator in Court second and assume their way into that relationship and pay the money.

**GLAZEBROOK J:**

But why is that absurd?

**MR CHESTERMAN:**

Because the money was never the company's to pay to its general creditors in the first place. It was never available for them.

**GLAZEBROOK J:**

Well here we don't know that, I suppose it comes back to Justice Kós' point, because it may well have been, although if MSH2 is in administration perhaps not.

**MR CHESTERMAN:**

But I think we've also got to just come back to the common evidence in this case and this will be part of my answer to your question, Your Honour, which is that the evidence at trial by the respondent's expert, Mr Hagen, was that there was no diminishment of the assets but he said, but the assets of the wider group were diminished and therefore they were worse off, and he was cross-examined on that, quite thoroughly, despite my learned friend's suggestion that I didn't. I said well there's no pooling application, you have no entitlement to that money, and his interpretation essentially from his perspective was that you should be able to look to the wider group when assessing a diminishment of assets. So he agreed there was no diminishment of NCI's assets and Mr McCloy who was for Robt. Jones Holdings, his evidence was there's no diminishment of the net assets and as a

result of swapping the creditors, none of the unsecured creditors were worse off. No one was worse off. So when Mr Hagen's replies to that evidence, his evidence is that it's trite that there is no diminishment in net assets but people were worse off, entities were worse off, and he doesn't mention NCI or its creditors, he talks about Columbus, which is another third party company which was dealing with these licences, and he talks about MSH2, and where this comes back to I suppose that could well decide the issue for Your Honours because my submission is that these are separate legal entities and the scope of liquidation is confined to the company itself and its transactions and it is dangerous to start looking at subsidiaries or related companies or other companies as having obligations to creditors.

**ARNOLD J:**
But this was a payment by the company, wasn't it, I thought that was –

**MR CHESTERMAN:**
Yes, so that's part of the test, it's written in the statute that it's a payment by the company and –

**ARNOLD J:**
Right, and it's accepted that this was a payment by the company, isn't it? Well it's been found –

**MR CHESTERMAN:**
In terms of the words of the, in terms of those words the common law on payment by the company is it must be at its direction or with its consent, but that law doesn't address whether it was an asset of the company or available for creditors, and it's not examining the disadvantage rule whatsoever, so that law is devoid of an analysis that includes disadvantage, and that's addressed in one of the commentaries I referred you to.

**ARNOLD J:**
Okay.

**MR CHESTERMAN:**

So in any case, so *Chatfield* was an ordinary course of business case. It didn't delve into the background for the legislation. It was not dealing with diminishment of assets. Within *Chatfield* it then referred to a case *Re Modern Terrazzo Limited (in liq)* [1998] 1 NZLR 160 (HC), once again that was not a diminishment of asset case. it was an ordinary course of business case and if I just take you to that, that's at volume 2, tab 19 , and the paragraph I will take you to is at page 169, and it begins at paragraph 15 onwards is talking about section 266 and it has (292), section 266 was a transitional provision that applied to the 1955 Act until all the companies came under the 1993 Act and at line 26 the Court refers to, "The aspect under challenge in s 266 is not liability as between creditor and company but payment in full achieved at the expense of other unsecured creditors." And I know Your Honour refers to that expense as being preferred, just because they were paid and others weren't, but my submission is that what that is talking about is causing detriment to those other creditors. And the other relevant passage is at page 174, line 35, where the Court refers to, "The primary focus now lies upon the effect of the payment rather than the motives which underlay it." And so this was an ordinary course of business case that was relied upon by *Levin* to support its conclusion that the disadvantage rule had been ousted.

The other case relied upon in *Chatfield* was *Countrywide Banking Corporation Ltd v Dean* [1997] 1 NZLR 385 (PC), which was a Privy Council case and that too was an ordinary course of business case and I'll refer Your Honours, within both *Countrywide v Dean* and within *Re Modern Terrazzo* they refer and place some weight upon an article by Matthew Conaglen, who now writes in the area of equity, but at this time was writing in the area of voidable transactions, so it's bundle 4, tab 6, the reason I'm taking Your Honours to this article is because it was given such weight in *Countrywide Banking Corporation v Dean* and *Terrazzo* for this principle that the ultimate, the section is not concerned with the ultimate effect, and if you turn to page 198 of the article, the article is specifically limited to the intention test. It's not the place to attempt a comprehensive discussion, instead he proposes to consider that part of section 309 which relates to intention of the debtor since

it's the part of the test for voidability which was most changed by the 1993 Act. And at page 204 of the article Mr Conaglen then refers to the reasons for reform as well. "The Commission said very little on voidable preferences, but clearly indicated disapproval of the then current reliance on the debtor's intention." And throughout the article at page 206 onwards confirms that the most striking alteration, this is page 206, four sentences down under "Transactions having a Preferential Effect", "The most striking alteration in s 292 has been the removal of the intention of the debtor as the central concern." So all of the materials that were being referred to in *Levin* were really confined to this intention issue and the ordinary course of business test that was within section 292 and they, *Levin* did not address cases that looked at the disadvantage rule or diminishment other than *National Bank v Coyle* which it overturned.

The other aspect of *Levin* is that it referred to Australian case law and in particular a case named *Walsh v Natra Pty Ltd* (2000) 1 VR 523 (CA) and I address this in my submissions already. The Court said that essentially the disadvantage rule no longer applies in Australia, but it was incorrect in saying that, and the passage put in *Levin* did not contain a very relevant sentence which confirmed that the passage was obiter. So when you do look at the Australian position, which I've set out chronologically in that extra sheet I handed up, it's quite unclear what the position is in Australia. But what is clear, in my submission, is the Harmer Report, and I took you to that first page of the Harmer Report and that was in, the first sentence refers to that protection against diminishment of assets rule.

**O'REGAN J:**
But the Australian case, *Federal Commissioner of Taxation v Kassem* [2012] FCAFC 124, (2012) 205 FCR 156 is almost identical to this case and has decided in favour of the liquidator, isn't it?

**MR CHESTERMAN:**
Yes.

**O'REGAN J:**

So although the Court of Appeal might have been wrong in *Levin*, they're not actually wrong overall are they, that if this case had come before the Federal Court of Australia you would have lost there as well?

**MR CHESTERMAN:**

Well, in my submission they could be right overall, they could be wrong, because we don't know really what the final position is in Australia. What we do know is at the date of *Levin* the Court of Appeal did not cite the correct position and that we know that it –

**O'REGAN J:**

Yes, but that's neither here nor there now, is it? I mean, what we want to know is is there support in the Australian law or not, and certainly my reading of *Kassem* is that it's exactly the same as this case and it goes against you. I mean, is there any difference between that case and this case?

**MR CHESTERMAN:**

Well, one of the differences, and I think it is something that I do wish to emphasise, is the evidence in our case. The common evidence was that there was not a diminishment of NCI's assets and those that were worse off were these outside entities. So that's the evidence we're dealing with in this case and that did not appear to be the evidence in –

**O'REGAN J:**

And that was the evidence they were dealing with in *Kassem* as well.

**MR CHESTERMAN:**

I don't believe that was the evidence in *Kassem.*

**GLAZEBROOK J:**

Well, shall we have a look at it? If you want to say why it's different let's have a look at it. Whereabouts is it?

**MR CHESTERMAN:**

That's at the respondent's volume of authorities at 7. So what I'm saying about *Kassem* is not that it is completely factually distinguishable, and the facts are very similar, if not identical to the current case except for the fact that the evidence in our case was that the transaction did not diminish the assets, and my point was that, from my reading of *Kassem*, that was there was no common position on that evidentially in that case. But *Kassem* did reject the disadvantage principle, and that's at page 163 to 164 of the judgment, and in my submission that was contrary to the High Court authority in Australia. But the reason that *Kassem* gave for finding that this loan was an asset of the company appears to be in essence that it was captured by the words "by the company", and that's at page 162, but it also provides reference to an authority, which is *Andrews v Australian and New Zealand Banking Group Limited* (2011) 6 BFRA 233 – just give me one moment, Your Honours…

**O'REGAN J:**

My only point was that you said the Court of Appeal on *Market Square* was wrong about Australian law and all I'm saying is it doesn't matter because Australian law now, at least in a case exactly the same as this, is as the Court of Appeal said it was, which is there is no need for diminishment. And, I mean, there is no answer to that, it's an identical case, I mean, there is no differences between them. It's a third party payment to a creditor treated as a payment by the company, the creditor was preferred and the Court said it had to pay the money back.

**MR CHESTERMAN:**

And what I'm saying is that the Court was not correct in its conclusion. First of all it dismissed the disadvantage rule, and my submission is that dismissing that rule is contrary to the Harmer Report, and there are a number of authorities in Australia that uphold the rule. Secondly, it referred to an authority, *Andrews v ANZ,* as authority for saying that the payment in this case was an asset of the company available for creditors – and I haven't brought a copy of *Andrews* with me, but if you look at that case it doesn't say what this Court uses it for. What *Andrews v ANZ* says is that an overdraft is

treated as a loan, it's not a voidable transaction case, it's not dealing with the diminishment principle, it's completely separate, it's dealing with a finding that an overdraft is a loan. So it appears to me that *Kassem* is not, well, first of all it's not binding because it's an Australian authority that departs from the Harmer Report but, secondly, it doesn't really give any real authority for why it considered this loan to be an asset of the company, and the one it does provide doesn't support it. So…

**O'REGAN J:**

So you'd say it's indistinguishable but it's wrong?

**MR CHESTERMAN:**

Yes. Except for the evidence in our case, Your Honour.

**O'REGAN J:**

Well…

**MR CHESTERMAN:**

Well, it's distinguishable in terms of the – I mean, the evidence is what it is, so…

**O'REGAN J:**

Yes. The third party payment's –

**MR CHESTERMAN:**

The overall structure…

**O'REGAN J:**

– exactly the same, a payment made at the direction of a company to a third party and the third party had to cough up, that's the outcome isn't it?

**MR CHESTERMAN:**

And that's what happened in *Levin* as well.

**O'REGAN J:**

Well, that's exactly – you were trying to tell us *Levin* was inconsistent with Australian authority. All I'm saying is it's completely on all fours with Australian authority.

**MR CHESTERMAN:**

But it's not, Your Honour. It might possibly be looked at of any Australian authority which rejects the disadvantage rule, but it's not going to be on all fours with any authority that uphold the rule.

**GLAZEBROOK J:**

Well, your point is the Australian authorities are not fixed and so if we want to harmonise with Australia we could choose one or the other because it's not clear what the answer is and we should choose the fundamental principle because that's been around since Lord Mansfield, that's the submission isn't it?

**MR CHESTERMAN:**

It is the submission, and that the position in Australia has gone astray from the very report that our legislature relied upon.

**GLAZEBROOK J:**

Alright. Well, I think we've got that point and you've got three minutes before 1 o'clock. So is there anything you want to say to sum up?

**MR CHESTERMAN:**

Why I asked the Court to focus on its decision is the fact that this was a principle that was around for a long time and was fundamental and that, in my submission, was not removed by Parliament. No system of law is perfect, there will always be problems with practical hypotheticals, cases overseas that find one way or another on a certain fact scenario. But we need to take a principled approach to this law and if there are problems with it that arise in scenarios, which, I submit, have not occurred in the over 250 years that the rule has applied, because no problems were mentioned by Parliament or

anyone else, that if problems do arise it's not the role of the Court to jump in and extinguish the principle as the *Levin* Court did, in my submission, it's the role of Parliament.

Those are my submissions, Your Honours.

**O'REGAN J:**

Well, hang on, sure a final Court can overturn a decision of a lower Court. It is our role to change. If we think it's wrong we should change it.

**MR CHESTERMAN:**

Well, no, I'm –

**O'REGAN J:**

I mean, if we disagree with *Lewis v Hyde* we should change it.

**MR CHESTERMAN:**

If this Court considers that the disadvantage rule was in place from the inception of the voidables regime in the 1750s right through until 1993, then that is a fundamental common law principle that this Court, and that rule remained, this is Court is not in a position to remove that principle –

**GLAZEBROOK J:**

Well, actually we can, if we think the law should be developed. We're actually talking about – there is the intervention of a statute and your argument –

**MR CHESTERMAN:**

Yes.

**GLAZEBROOK J:**

– is that Parliament must have enacted the legislation knowing that that was the rule and that that carries on. But if you were just looking at a purely common law rule we can actually do what we like in respect of that rule. We may decide it's not wise because there are commercial uncertainties but

we can do it. But I think your argument is something different, you are saying that because of the intervention of the statute that has always been interpreted as being subject to that rule and Parliament hasn't said anything to suggest that they're overturning it, it must have carried on into section 292.

**MR CHESTERMAN:**
That's right, and I accept of course it's the Court's role to develop the law, but this would be more than a development, it would be the extinguishment, confirmation that the Court was entitled to completely extinguish the common law rule.

**GLAZEBROOK J:**
Well, I think we probably are, and in many cases have. For instance that taxation statutes should be construed narrowly, the Courts have done away with that, penal statutes should be construed narrowly, might have had a slight nudge-on from Parliament but actually not before that was decided. And in any event, we will give you, we'll break for the adjournment now because there may be, we can give maybe 15, up to 15 minutes after the, so to 2.30, if there are any points, but only if there are points that you haven't dealt with rather than just repeating the points that we do understand.

**MR CHESTERMAN:**
Thank you, Your Honour.

**GLAZEBROOK J:**
So we'll take the adjournment.

**COURT ADJOURNS: 1.01 PM**

**COURT RESUMES: 2.17 PM**

**MR CHESTERMAN:**
May it please Your Honours. I hope to wind up within about five minutes, less than 10 minutes, and just to provide a summary. It's my submission that the

first point I've attempted to make today is that the diminishment rule existed since the foundation of the regime. The second is that it applied under section 309 of the ’55 Act, even though it was never explicitly mentioned in that Act, or in any previous Act. The third point is that there’s no evidence of a desire of Parliament to remove this concept from the regime, and I took you through the relevant reports and referred to the debates. The fourth is that the rule continued beyond the enactment of section 292 because it was held to apply in *National Bank v Coyle*, which was several years after the enactment of section 292 and it was, in fact, in 2011 when the *Levin* court found that the rule no longer applied. The fifth point is that the *Levin* court extinguished the rule, in my submission, without deference to Parliamentary intention and debates, and relied on cases to say disadvantage no longer applied but those cases did not stand for that principle. The sixth point is that my submission is *Levin* was wrong to depart from that line, which was established by Lord Mansfield, and carried right through to *National Bank v Coyle*. And I do accept Justice Glazebrook of course that this court may use its powers to find that policy dictates that the rule should be abolished. However, what I say is that the Court should not do that because it existed without practical issue for a very long time. The rule is not absurd. If it did not exist then situations such as this, where the pool of assets increases post-reversal would occur. The UK, Canada and Scotland have seen fit for the rule to continue, and in particular, keeping in mind that our regime derives from the UK. It is also logical to care about disadvantage. If an advantage is required it must logically encompass some corresponding disadvantage on the other side.

Yes, this factual situation might be rare, but it’s not trivial for the Courts to consider because it is one which I suppose gives life to the underlying purpose behind the regime and when Your Honour asked me about the policy behind the rule, my response to that is, disadvantage is a key purpose behind the regime, and that’s the opening paragraph from the *Allied Concrete* case. I'll just read that paragraph. It says, “On the one hand, a key purpose of the voidable transaction regime is to protect an insolvent company’s creditors as a whole against a diminution of the assets available to them resulting from a transaction

which confers an inappropriate advantage on one creditor by allowing that creditor to recover more than it would in a liquidation." So it is a key purpose of the regime.

When we talk about policies they are something different from purpose, in my submission. A purpose is the reason for which something exists, for which the legislation was enacted. It describes the mischief. A policy is an objective, that maybe a competing policy. It's not necessarily in all cases for legislation to be interpreted consistently with one policy, but in my submission the legislation must always be interpreted in light of the key purpose of the legislation.

The *Allied Concrete* case, although I do accept that it is of course different, it dealt with the continuing business relationship defence and whether or not a creditor should give value at the time of payment, and that was the factual matrix for that decision, but the Court in assessing that did delve into the, it went thoroughly through the background to the regime and the legislative developments, including 1993 and 2006, and in my submission although of course the Court was speaking in terms of the specific defence it was looking at, the Court did make some comments which do shed some light perhaps on the rule that the appellant is asking be implemented. The Court said at 56 that there was a stark choice for the Court. Primacy to creditors as a whole versus primacy to individual creditors. That was at paragraph 55. And that in a sense does come into play here where the view of collective realisation and equal treatment on the one hand, versus the appellant's position that the diminution rule exists and the individual creditor should be able to retain the money. So that's, in my submission, a stark choice for this court as well.

The Court then at paragraph 95 addressed the Court of Appeal's assessment of the policy behind the regime and it referred to the Court of Appeal as describing the voidable preference regime as an attempt to strike a balance between the interests of all creditors in being able to share the assets of the company and the interests of particular creditors who believe they have a valid defence. But the Court of Appeal went on to say that, "The objective and

effect of the regime was not to do justice or achieve fairness between a particular creditor and the debtor company, but instead to achieve fairness among all creditors inter se."

Now the Supreme Court expressly disagreed with that. It said, " As the material we have cited from the legislative background127 and the explanatory note to the Companies Amendment Bill 2006 demonstrates, both the Government and Parliament understood that there was a conflict between the concept of collective realisation and individual justice in particular cases and accepted that, in some circumstances, the need for individual justice would prevail over the underlying policy of collective realisation." And in my submission where you have a case which meets the underlying purpose of the regime, or is protected by the underlying purpose, that is a situation where collective realisation must bow down.

**GLAZEBROOK J:**

So you accept, as I understand it, that actually conflicts with the pari passu rule? That's what you said before, that we had to choose between pari passu and otherwise, and I was going to say to you but at least one of those reports said pari passu is the reason for the rule, at least in the new rule.

**MR CHESTERMAN:**

My position, Your Honour, is I do not consider the rules, the concepts conflicting. The way I have approached the disadvantage rule is that it is an underlying requirement for any voidable transaction before there is even any consideration of equal treatment. So in that sense it's my submission that there isn't conflict. However, if the Court considers that the disadvantage rule is not the underlying purpose of the regime but is a mere policy objective as the Court of Appeal said, then my submission is that if the Court considers there is a conflict my submission is that that should give way to the disadvantage rule.

The Supreme Court also went on to address the submission that the 2006 reform had significantly curtained a defence that was available, and the Court

was addressing a comparable situation in Australia. And at paragraph 100 the Supreme Court said that there is nothing in the background material to suggest that this was intended, ie, Parliament to curtail the scope of the –

**O'REGAN J:**
Could you just give me the paragraph number again?

**MR CHESTERMAN:**
Yes, that's paragraph 100, nothing in it to curtail. And that relates –

**GLAZEBROOK J:**
Nothing in it to curtail what, sorry?

**MR CHESTERMAN:**
To curtail the scope of the defence that was being considered in that case. And the Court then went on, because the argument being advanced in that case was that a different meaning should be ascribed to the words than should be given to the equivalent Australian provision, and the Court at paragraph 102 – and again I'm aware that this relates to this defence and I'll relate it back to ours – paragraph 102 said that if a different meaning was to be ascribed to the words in section 296(3) to Australian wording that would have been, "Explicitly signalled at some point in the background materials, given the extensive discussion that preceded the introduction of the Insolvency Law Reform Bill in 2006. But we have seen nothing in the materials to indicate such an intention." If the Court of Appeal was right then, "Parliament effected a fundamental change in policy as against the position in Australia, but one that was, as far as we have been able to ascertain, unheralded." And my submission is coming back to the Harmer Report that I took you to where I interpreted that first page of the report as explicitly recognising that diminishment of asset remained as a key purpose, and my submission is that if the disadvantage rule was curtailed by Parliament and if the *Levin* Court was correct, then it was a significant and fundamental change in voidable transaction law that was unheralded by Parliament.

The final point I wish to mention is that *Allied Concrete* – and now at paragraph 174 – there is reference to the history of the regime and it said, "In my view, the history of the voidable preference statutes referred to and the fixed purpose of the legislation in recognising the need for balance between the interests of the pool of creditors on insolvency and the needs of commerce in permitting transactions in the normal course," and it goes on at line 11 to say, "Such change is contrary to the fixed policy in protecting ordinary business dealings which has been followed by the law since Lord Mansfield. There is nothing in the immediate legislative history of the 2006 reforms to suggest any statutory purpose in removing protection," from these commercial dealings that were at issue. And so my submission here is that in *Allied Concrete* the Court saw fit when interpreting the defence to go back to the original principles founded in Lord Mansfield's early judgments, and it's my submission that those principles should be gone back to here and given appropriate weight.

Those are the submissions for the appellant. Thank you for your time.

**GLAZEBROOK J:**
Thank you very much, Mr Chesterman. Mr Keene.

**MR KEENE QC:**
May it please the Court. Does the Court wish to read the synopses and then I can speak to them very briefly?

**GLAZEBROOK J:**
I think just start off. But don't read the synopses, you can speak to the synopses.

**MR KEENE QC:**
The pathway taken by the respondent is to address the question submitted by the Court for answer and we, in paragraph 1, accept as an assumption but not a concession that arrangement with MSH2 and Northern Crest was a loan. The reasoning of the Judge at first instance, Justice Gordon, and Winkelmann

in the Court of Appeal, is common except for the difference between whether the nature of the MSH2 arrangement was a repayment in redirection of fees, whereas Justice Gordon took the view it was a loan.

So we move from there, paragraph 3, the job of the Court is to interpret and apply the words themselves and, while my friend has done very diligently work upon various academic commentaries and reports preparatory to making changes to the law, at the end of it the Court needs to apply the words of the section, and I won't take any further time about the disadvantage rule as a, quote, "common law element", because that's not what the Courts are asked to interpret.

In the leave reasons the Court explained that the approved question was framed to permit the appellant to argue that a payment of the company is an insolvent transaction. Diminishment of assets, available to creditors, must also be proved in addition to section 292(2)(b) test, which I have described as the received law test. In that respect it would make little sense to have a threshold test to apply to the application of the section when the section itself contains within it the very same test. So one then asks what is the in-addition need if, having got to the test within the Act and received more, then the section would apply because of section 292(2)(b). So "received more" indicates that a creditor has received something which his like creditors has not received. Where does that come from? The answer must be from the pool available to the creditors. So if the pool available to the creditors is the source of the payment which the impugned transaction looks at, we must say that there is diminishment because diminishment is something that relates to the distribution and is central to pari passu.

Now my friend sought to argue that pari passu was not the principle intent of the section but in my submission that submission is not tenable. It is also fair to say that the payments were not ones that could include, in my submission, the loans that have been made on the assumption which I have already conceded because although they may be transactions, the loans themselves could never be impugned under the section because a loan is a payment

which doesn’t cause there to be any diminution. What is being talked about in the section is steps taken by the insolvent company to make payments. Payments to it are not within the section. So as far as we are concerned we say that the loans are not susceptible to the regime because they are an accretion of assets, in this particular case, $260,000 worth of money.

**O’REGAN J:**

Well except there was never a time when Northern Crest had that money in its hand is there. If the payment was made directly by MSH2 to RJH.

**MR KEENE QC:**

Yes that is so.

**O’REGAN J:**

So the payment and the loan are, in fact, a single transaction aren’t they?

**MR KEENE QC:**

They are in my submission not a single insolvent transaction, for the reasons I've just given.

**O’REGAN J:**

It doesn’t matter, does it. If it’s a single transaction the fact is the pool of assets was never increased by the amount lent by MSH2 to Northern Crest, and therefore couldn’t have been reduced by the payment made by Northern Crest to RJH.

**MR KEENE QC:**

Well that is true in relation to the loan but it is not true necessarily, in my submission, in relation to the overall transaction because, and now we come to the issues which His Honour Justice Kós has raised, and that issue is we have a wholly owned subsidiary that has paid $260,000-odd and even if what one says is it didn’t arrive in the bank account of Northern Crest, one can say definitely that it departed MSH2 and MSH2, being a wholly owned subsidiary, at any time would either obey the direction of Northern Crest or alternatively

be realised and that realisation would be likely to, and I'll come to some numbers shortly, be likely to have provided a return to the other creditors. So whilst what Your Honour has put to me is true, the issue about diminishment actually works on two levels. The first level is to say if you accept that there was a loan then you accept that the asset that is part of the loan became something which was capable of being dealt with under the instruction of Northern Crest, and it was so dealt with, and it therefore reduced the amount payable to Northern Crest. But if it is a loan there is nothing to suggest that it should not be treated as any other asset. It may well be that one says, well, because this has happened directly between MSH2 and NCIL there is a difference there. In my submission that is an assumption and not necessarily a matter of proof.

**O'REGAN J:**

Well, was there any expert evidence on that? I mean, it seems to me that the payment by MSH2 to RJH, that was then reconciled in the accounts as being an advance made to NC and then for NC paying RJH.

**MR KEENE QC:**

Yes.

**O'REGAN J:**

But that was only an ex post facto accounting entry, there was never a moment where the money lent by MSH2 was actually Northern Crest's asset.

**MR KEENE QC:**

No, that is true, but it doesn't, in my submission, affect the way in which we need to look at this because if there is a loan it is an accretion of an asset by Northern Crest that paid off a debt, and that was the direction that the sole director of MSH2, the subsidiary, gave and that's what happened. Whether it was a necessary part of any different or grand scheme, there is no evidence because we were not blest with the reliable evidence of Mr Eakin, who preferred to remain in Australia at the time. So the assumption could be it went through because that was the safest way or, alternatively, it could just be

a matter of convenience, and it should be borne in mind that the whole of this time over which these MSH2 payments were made there was ferocious steps being taken by Robt. Jones threatening to attack Northern Crest who, at the time, was trying to relist on the Australian stock exchange. So it's not beyond the range of surmise to say that as soon as they had got together what they were going to do they made sure it went straight across and didn't do it in two hops. So –

**O'REGAN J:**

Well, it doesn't matter why they did it, the fact is they did do it. That's the reality we're facing.

**MR KEENE QC:**

Yes.

**O'REGAN J:**

That there was a direct payment. You're saying we have to pretend that there is actually a loan to Northern Crest, an accretion of Northern Crest's assets as a result of that loan, and then a diminution of those assets as a result of the payment to RHJ.

**MR KEENE QC:**

But if the accounting records inside of MSH2 and Northern Crest say it was a loan and if I accept for the purpose of answering the question as put that it was a loan, then isn't that game, set and match for the accretion of the asset? It may well be that it then went straight off, but there are two elements and in my submission –

**O'REGAN J:**

Well, I don't agree, there weren't two elements, there was one payment, and it didn't go through Northern Crest. There was then an ex post facto rationalisation of what had occurred to establish the debt owed by Northern Crest to MSH2.

**MR KEENE QC:**

I understand that, but if we are to assume that it was a loan – and that's effectively what we have done in order to deal with the question – why is that not an accretion to the assets by –

**O'REGAN J:**

Because the very act of making the loan also decreased them, so they never went up, they didn't go up so they couldn't go down.

**MR KEENE QC:**

Well, they retired debt and that, if one looks at the net assets available to creditors, means that you would have to have said that there was no other way that loan could have been approved except for that purpose.

**O'REGAN J:**

Well, no, you don't, you just take what's in front of you. In this case we had RJH owed 260,000 and then a scintilla of a second later we had MSH2 owed 260,000. But the pool of asset available to the unsecured creditors at all times remained the same, that's the argument you're facing.

**MR KEENE QC:**

Well, let's just take that situation and my submission would be this. The test is from the point of view of the creditors at any given point in time, if there is a diminution and one creditor receives more, and there can be no doubt that Robt. Jones received more, what has happened is that the more is deemed to have been something that is available to all creditors –

**O'REGAN J:**

Why? The more came from a third party, it had nothing to do with Northern Crest, it came from MSH2.

**MR KEENE QC:**

Well, in my submission, if the loan is treated as being a loan by Northern Crest, then it has come from Northern Crest and it has come from

Northern Crest's coffer, if I can put it that way, represented by MSH2. What you've got left then at the end of that exercise is that MSH2 is a creditor following the transaction in respect of the 260,000, and that 260,000 amount, if you take the counterfactual and say, well, it might have never happened, you find that the money has actually gone to one person. If the counterfactual had applied and it hadn't been paid it would be a sum of money sitting available –

**O'REGAN J:**

No, it wouldn't, it would be sitting in MSH2, it wouldn't be available to the creditors at all. If it didn't happen the money would have stayed in MSH2.

**MR KEENE QC:**

Well, I was about say what Your Honour has just said, and I don't have any difficulty with that proposition. But what I will say is that MSH2 as an entity, as a fully owned subsidiary, would be worth a greater sum then it was after the entry. So the idea –

**GLAZEBROOK J:**

Well, it might depend on what other creditors there were, I suppose.

**MR KEENE QC:**

Yes, and I'll point Your Honours to some numbers about that shortly.

**GLAZEBROOK J:**

Okay.

**KÓS J:**

And your point, as I understand it, is you are distinguishing MSH2 from a true volunteer.

**MR KEENE QC:**

Yes.

**KÓS J:**

The fact is a payment was made by MSH2 to RJH at Northern Crest's direction.

**MR KEENE QC:**

Yes.

**KÓS J:**

MSH2 was not a volunteer, it took that step in response to a direction from its shareholder.

**MR KEENE QC:**

Yes, that's the evidence.

**KÓS J:**

And then you also say, and it seems to me a stronger argument for you than the one you've made, that there is a difference then in the net worth of the assets of Northern Crest as a result of that transaction.

**MR KEENE QC:**

Exactly, yes.

**KÓS J:**

So can you show us how that is the case?

**MR KEENE QC:**

You want the numbers now?

**KÓS J:**

Yes, well I would.

**MR KEENE QC:**

Yes, let's –

**O'REGAN J:**

I must say this is a different argument than the one that you and I have been debating, isn't it.

**GLAZEBROOK J:**

Yes, well I think put at your highest though your argument is that because it's actually treated as a payment from Northern Crest, despite having come from MSH2, under the section 292, then in fact whether it's come from a third party or wherever it's come from, it actually is a diminution in assets.

**MR KEENE QC:**

Yes.

**GLAZEBROOK J:**

Because of the way that 292 is structured. So you've got about a four tier argument as I understand it. One, that it doesn't matter if it's come from a third party because you're looking at the payment from Northern Crest which is under 292 and by its very nature, because it's a payment from Northern Crest it's a diminution of the assets available, even if it in fact came from a third party and the third party had no obligation to make it. I think the second tier of your argument is what you were saying, what Justice Kós just said, because it's come from the subsidiary, a direction, then they've directed it to come through, they could easily have directed it to go directly through and therefore again it's a diminution. And the third one is, that it's actually a diminution because it's diminished the assets of the wholly owned subsidiary that would otherwise have been available to Northern Crest in any event.

**MR KEENE QC:**

Yes.

**GLAZEBROOK J:**

Is that, however that might be, either through direction or through liquidation of MSH2.

**MR KEENE QC:**
Yes, and there is a further element to it which may well be incorporated in your four part summary.

**GLAZEBROOK J:**
It might be.

**MR KEENE QC:**
And that element is that there is a loss of value of some sort of MSH2 as an asset of NCIL but on the other hand the group of creditors as a whole, treated as one creditor, finds itself that the sum of money, the $260,000, has gone to someone who has received more, and because –

**GLAZEBROOK J:**
Well that presumably is saying well that's all the section says. If it's a payment where somebody receives more then that quite clearly means that the pari passu rule and the clear words of the statute are breached and that's the end of it.

**MR KEENE QC:**
Yes. That –

**GLAZEBROOK J:**
And it doesn't matter about diminution or anything to do with it, they've just received more and that's what the section's about.

**MR KEENE QC:**
Yes, that's right. Well I do think that my friend made quite a set of strong submissions talking about effectively the diminution principle and all I can say is that once there has been the satisfaction of 292(2)(b), where someone has received more, that ipso facto actdually honours the diminution principle. So there's no need as the question asked by the Court presumes for us to have an additional test because the test is within 292(2)(b) anyway.

I think I've dealt with paragraphs 5 and 6 of the synopsis. All I suppose I'm saying, subject to the reservation which His Honour Justice O'Regan has relating to the direct payment, said that the Court should approach the transaction as though it were the same as the Columbus loan. In fact if we did get to the notion of trying to decide how the transaction should be properly dealt with in the sense of redirection of fees et cetera, there would be strong arguments in relation to redirection of fees.

Onto paragraph 7, I think that's been dealt with as well. I have incidentally made available to the Court, I presume it's come, to the notice to set aside, and I make it clear that notice focuses upon the payments and not upon the loan and again I accept Justice O'Regan's qualification to that, but nonetheless that is what is the impugned payment, or payments.

So having looked at the approved question, and I say at paragraph 11, it would be odd that the common law can operate to add a threshold test to the statute so that it fundamentally changes and even negates the plain and clear principle objective of voidable transactions, namely pari passu, and in my submission that is in effect what would happen. Second, there is authority that the receive more test implies diminishment of the net assets available to creditors. Diminishment here is not defined by the rules of double-entry bookkeeping. Rather it's governed by the premise that Robt. Jones payments to which 292 applies result in less being available to the creditors seen as one entity. That notion of the creditors being seen as one entity, and knowing that some, one person has stolen a march, is an important part of the voidable transaction view. It is not a question whether the net assets per se has changed. The question is has the net assets available to the creditors, as though they were one creditor diminished, and in this case my submission is it has.

Then in paragraph 14 Robt. Jones of course clearly received more from the insolvent transactions and that more could have been available to the general creditors. In arguing there is no, I am in paragraph 15 now, in arguing there is no diminution of assets and therefore no harm to creditors, the appellant

misconstrues the transaction as being not payments of Northern Crest to Robt. Jones, contrary to paragraph 1 of the Court's reasons, but rather a simple replacement of Robt. Jones by MSH2 as a creditor. MSH2 did not acquire the Robt. Jones debt. rather it loaned money to Northern Crest to allow Robt. Jones debt to be extinguished, and that is an important difference in my submission. The transactions are plainly and simply payments of Northern Crest sourced from MSH2 although the liquidators advanced arguments that MSH2 money was paid by MSH2. In the end the High Court preferred the view that MSH2 money was a loan and the Court of Appeal accepted that MSH2 money could have been a redirection of fees or a loan. In either case the payments from MSH2 would fall within the established category of cases where the payments would be caught as payments by the company for the purpose of 292. The payments were intended and did discharge Northern Crest's debt to Robt. Jones.

MSH2 is a wholly owned subsidiary of Northern Crest controlled by Mr Eakin if sole director was directed to make the payment the source of which was evident to Robt. Jones. The cash so transferred, the $262,000, was sufficient to pay off the Northern Crest debt. Inevitably the valuation of MSH2 as an asset of Northern Crest will have reduced by the dissipation of that 262,000.

**O'REGAN J:**
Well not necessarily. I mean MSH2, if MSH2 borrowed that money, and paid it to Robt. Jones, there wouldn't have been any change in its value. It all depends on what the assets of MSH2 are. I mean if MSH2 was a hopeless basket case worth zero all this means is it was more emphatically worth zero.

**MR KEENE QC:**
Well perhaps I'll address those numbers now. I refer Your Honours to case on appeal volume 5 and starting at page 1075. This is a balance sheet of MSH2 as at the date of its going into administration. So this is post all of the payments which this court is considering, and it can be seen that the current assets, non-current assets and total assets have respective figures, and that the net assets would seem to be $950. That is post the –

**GLAZEBROOK J:**

Where's that sorry?

**O'REGAN J:**

That's in brackets so that's a net liability.

**MR KEENE QC:**

Yes, net liability.

**ELLEN FRANCE J:**

Of 960 is it?

**MR KEENE QC:**

Yes, 960.

**O'REGAN J:**

We really need to know what was MSH2's position immediately before it made this payment and where did it source the payment from.

**MR KEENE QC:**

Yes well I'm not able to…

**GLAZEBROOK J:**

That's a current ratio in working capital.

**O'REGAN J:**

Yes, but it's after the payment was made.

**GLAZEBROOK J:**

Yes, I know, but we've got the balance sheet after the payment was made, it's just 7000, minus 7000. Or minus 960.

**O'REGAN J:**

No that was –

**GLAZEBROOK J:**

Minus 960, all right, so that's after the payment's made.

**O'REGAN J:**

In the previous year it was also in the red.

**GLAZEBROOK J:**

And more.

**O'REGAN J:**

So it does seem to have been a company that was insolvent the year before, made this payment, it was still insolvent, so it was worth nothing before and it was worth nothing afterwards, so there is no diminution in the assets of Northern Crest, is there, it's just gone from being a worthless company to a slightly more worthless company.

**KÓS J:**

Doesn't that depend on where the money came from that it paid on, and as I understood Mr McCloy's evidence it was that the payments came from revenue received by MSH2.

**MR KEENE QC:**

That is my understanding but I'll just see if my learned junior can help me with…

**KÓS J:**

I mean Justice O'Regan's point is absolutely right. If MSH2 simply borrowed the money and simply added thereby to its hopeless indebtedness. It was then worth nothing to Northern Crest and was worth even more nothing if it borrowed more. But if it had assets and paid those assets out to RJH, the position might be different.

**MR KEENE QC:**

All I can say this tells you is that after the payment of 260,000 its net assets were minus $950. So there's no sign of current liabilities or if you add the total liabilities together – can I take Your Honours to case on appeal volume 5 and go to page 1348. This is a set of –

**GLAZEBROOK J:**

It must be volume 6.

**MR KEENE QC:**

Volume 5 case on appeal. Sorry, it should be 214.

**O'REGAN J:**

No, that doesn't work either.

**MR KEENE QC:**

Sorry, it should be 1138. This is the account transactions for MSH2 between 1st of April 2009 and 2 June 2011 and what shows here is a series of quite significant payments coming from Columbus to MSH2. So it shows a fairly healthy set of payments in that period and those payments arise out of the licence agreement between MSH2 and Columbus and that agreement is in volume 4 of the case on appeal at page 147. So the picture appears to be that income was coming in at that time and –

**O'REGAN J:**

Could you just tell me the page number of the licence agreement again?

**MR KEENE QC:**

Page 147 in volume 4. The questions which the members of the Court have raised are very adroit and clear questions. The difficulty is in representing liquidators they get such financial information as they can draw from people who are reluctant and so we can only give you an outline of what was probably happening.

**O'REGAN J:**

Is there any finding of fact made in the High Court about the source of the payment made by MSH2, whether it came from borrowings or income or other fixed assets or…

**MR KEENE QC:**

No, there's no such finding.

**GLAZEBROOK J:**

Well, it's probably by the by anyway, because the argument would be that the net assets were reduced because the value of the company was reduced, i.e. and that's to the shares. But it might actually be an indication that this is far too much detail to go into, for a liquidator or anybody.

**MR KEENE QC:**

Yes.

**O'REGAN J:**

Well, I don't think we're in a position to make that finding. We're not in a position to make a finding that the value of MSH2 as an asset of Northern Crest was adversely, well, diminished by the payment made by MSH2 to Robt. Jones.

**GLAZEBROOK J:**

Well, especially looking at the balance sheet that was worse the year before than it was the year afterwards.

**MR KEENE QC:**

Well, I can only give the Court the information which I have…

**KÓS J:**

I mean, we have Mr Hagen's evidence of that diminished value, but it's rather an impressionistic rather than reasoned conclusion and it doesn't look like anyone enquired.

**GLAZEBROOK J:**

Well, probably because there wasn't any information upon which to base anything, one assumes, if you're looking at this, which is not a criticism of the evidence or the liquidators. As you say, you work with what you can manage to glean.

**MR KEENE QC:**

Yes. Well, you can't exclude full borrowing, you have information which indicates reasonably considerable sums coming in from Columbus. The question is is it more likely than not that there was a diminution, and in my submission the answer to that question is yes.

I pass now from the summary but indicate to you that at paragraph 21 I have raised what I've described as a floodgates risk which Your Honour Justice O'Regan said that if the arguments of the appellant were accepted there would be so many ways of getting around things it may in fact eviscerate the whole purpose of the voidable transaction section and –

**GLAZEBROOK J:**

What's said against you on that is these practical problems haven't shown themselves yet, and it's been around since Lord Mansfield. So do you have a submission on that? That's as I understood the submission.

**MR KEENE QC:**

Well, I suppose that one can say that cases have been around since Lord Mansfield's time but what do we know of ones where these issues have been looked at by liquidators and, if they are savvy enough to know what the problem is and see that there is a situation that might have applied to Lord Mansfield's test said, "We're not going to have a go at this because it going to cost a lot of money and we'll lose, or we may lose." So the answer to Your Honour is that the diminishment test, either within 292 or outside of it, is something of a risk taken by liquidators and in liquidations where they are small, there's little money, that no one is prepared to take the risk. You see one doesn't know the blockage effect of such things.

**GLAZEBROOK J:**
So what you're saying is that the regime beforehand was so difficult in any event to claw back preferences that in many instances it wouldn't have been done in any event and effectively that was one of the purposes of 292, to make it easier?

**MR KEENE QC:**
Exactly. It's clearer because it's very clear if someone's got some more and it's a very simple test and, in my submission, a true litmus test.

**GLAZEBROOK J:**
And then that it would take away from that if you were able to, by easy means such as directing third parties to pay, to get around that, especially if you can direct subsidiaries too.

**MR KEENE QC:**
Yes. Now at paragraph 21 I mention the floodgates risk. With the Court's leave I'll ask my learned junior to present about some of what those risk would be. But the risks include the implications and reactions that are possible out of accepting the appellant's argument, so it's not just looking at other risks.

Now what I'd like to do now is to briefly address some of the issues which my friend has raised to give a view of where the respondent sees some of those issues. I think that one of the objections which he raised is that if this sort of transaction is allowed then it will be a windfall to the other creditors because they would never have got the money, and I think the answer to that is, first, so what, but second, so what in the sense that what we're trying to do is to stop the practice and make recoveries when it happens. And the second thing is that if there were some value inside of MSH2 and if the liquidation had occurred at the time, they would have got some part of that money, and again it's an evidence matter that we have some difficulty with but nonetheless it's not in the nature of a windfall if the sort of picture I'm endeavouring to paint of MSH2 is correct.

There was talk of agreement between the experts in relation to the net assets, and I'd like to take Your Honours to, first, case on appeal volume 3, page 646. This is the evidence of Mr McCloy. He was under cross-examination and if you go to four lines from the top the cross-examination starts, "So the body of creditors in NCIL is no worse off," taking his earlier evidence, and then:

Question, "You as an insolvency practitioner would be aware of the provisions of section 292. That's the voidable preference section?"
Answer, "Yes, yes."
Question, "In section 292(2) there is a statutory definition of an insolvent transaction. Are you aware about that – of that?"
Answer, "Yes."
Question, "And doesn't it say that the second test is it enables another person to receive more towards the satisfaction of a debt owed by the company than that person would receive or would be likely to receive in the company's liquidation?"
Answer, "Yes."
Question, "Are you aware of that?"
Answer, "Yes."
Question, "Do you accept that Robert Jones received more than a like creditor because of these payments than anyone else?"
Answer, "That's the fact isn't it? Yes."

**O'REGAN J:**

That doesn't really take us anywhere. I mean everybody knows that. He would have, he had to accept that, didn't he, that's what all the …

**MR KEENE QC:**

Yes, that's right.

**O'REGAN J:**

Everybody else got zero and Robt. Jones got 260,000.

**MR KEENE QC:**

And –

**O'REGAN J:**

But that doesn't really help us, does it, in terms of answering the question that's before us, because I think Mr Chesterman accepts that.

**MR KEENE QC:**

Yes, yes, I am aware of that, but what I guess I'm trying to build on is the question of how that affects the net asset position. As I've already said the issue is not the net assets in a bookkeeping basis but the net assets –

**O'REGAN J:**

It's not net assets at all. If it was net assets section 292 would never apply. It has to be the gross assets. If you're talking about net assets, as soon as you pay a liability you reduce the assets, but you also reduce the liability, so the net assets always remain the same. So what we're talking about is the pool of assets available to unsecured creditors, but it's not net assets.

**MR KEENE QC:**

Well –

**GLAZEBROOK J:**

It's not even really gross assets because they're not going to be available to it, that is a round robin, isn't it.

**O'REGAN J:**

Yes.

**MR KEENE QC:**

It is probably a term that relates to the particular position of the company in terms of realisable assets.

**GLAZEBROOK J:**

Oh that might be right, yes.

**O'REGAN J:**

I think it's just the assets that in a liquidation would be available to the unsecured creditors i.e. aren't taken by a secured creditor or by someone having a prior claim.

**GLAZEBROOK J:**

Or preferential creditors, yes.

**MR KEENE QC:**

And where I think Mr McCloy got to was talking about net assets and when we get to, and I'd like to refer Your Honours to case on appeal volume 2, page 391. At paragraph 16 at the top of the page. The evidence of Mr Hagen, at paragraph 16, 17 and 18, made it clear that his view was that there's no doubt on the facts as explained by Mr Kerr and Mr McCloy that RJHL is very much better off than it would have been in a liquidation and further NCIL as a group is worse off.

**KÓS J:**

Well that's the impressionistic conclusion that I referred to before. It's not a very reasoned one.

**MR KEENE QC:**

It's an impressionistic conclusion. It's, I've given you all I can about hard information if you call the information arising from the MYOB accounts as hard information.

**GLAZEBROOK J:**

I suppose you say they're further into debt because they've paid out money they didn't have, assuming that MSH2 was as insolvent as it looks like, they've paid out money that they didn't have to a third party and so they're even further in debt than they were before, as a group.

**MR KEENE QC:**

Yes, that is so.

**GLAZEBROOK J:**

Because money's gone out of the group to somebody totally separate so they were minus whatever before and they're minus an extra 260,000 now.

**MR KEENE QC:**

Yes.

**GLAZEBROOK J:**

And in that sense it must be true.

**MR KEENE QC:**

Yes.

**KÓS J:**

But the question surely is whether MSH2 is worth anything at all.

**GLAZEBROOK J:**

Well no but it's all, even assuming it's not worth anything at all, that it's worth minus say 100,000, having paid out 200,000, it's now worth minus 300,000.

**O'REGAN J:**

But I mean saying that the group is worse off is begging the issue of whether the pool of assets available to unsecured creditors in a liquidation of NC would have been diminished by this payment. It's just, he's just talking at a parallel universe about the group. We've got to look at the company.

**MR KEENE QC:**

Taking up Justice Glazebrook's issue, whatever happens there was a diminution because MSH2 had enough money, by whatever means, to pay the 260,000 and what MSH2 got for it was an ability to prove for a debt for that sum that was worth nil.

**GLAZEBROOK J:**

Well it didn't actually. Can you give any other indication as to why it couldn't prove in the liquidation. Was it a set-off as Mr Chesterman thought?

**MR KEENE QC:**

Yes, I'll deal with that right now. MSH2 made a claim on the liquidators of Northern Crest. Northern Crest rejected that claim because the amount of indebtedness at the date of liquidation was considerable greater than the proof of debt, so they set it off.

**GLAZEBROOK J:**

It was a set-off.

**MR KEENE QC:**

Yes, yes.

**GLAZEBROOK J:**

Thank you.

**O'REGAN J:**

So actually if that's right the payment made by MSH2 to Robt. Jones shouldn't have been treated as a loan, it should have been treated as a reduction in the debt owed by MSH2 to Northern Crest, shouldn't it?

**MR KEENE QC:**

That's the reason for my saying that if we go to the next level of hearing there is quite a lot of information about the movement of monies between those subsidiaries and also Columbus because Columbus was making payments under the licence agreement and the result of that would be a submission rather like Your Honour has presaged.

**GLAZEBROOK J:**

But that might be a diminution in assets then, isn't it?

**MR KEENE QC:**

Well –

**GLAZEBROOK J:**

Of course that all assumes MSH2 had the wherewithal to pay anything which it didn’t seem to have.

**MR KEENE QC:**

Well, I agree with His Honour Justice Kós that maybe Mr Hagen’s views might have been impressionistic, if I can put it that way, as opposed to subject of detailed –

**GLAZEBROOK J:**

Well, I remember some of the things we were referred to in terms of commentary were saying that this didn’t apply if there was a set-off, and if there is a set-off in this case then the diminution of assets doesn’t apply, because presumably there is a diminution of assets because you reduce the asset that you have, being the loan owed by the third party.

**MR KEENE QC:**

Yes, well…

**GLAZEBROOK J:**

So if you borrow money from a third party to pay Paul but in fact you're owed a whole lot of money by the third party, then that will diminish the value of that loan because of the set-off.

**MR KEENE QC:**

Well, yes, except that that chases its own tail a bit, doesn’t it?

**GLAZEBROOK J:**

Well, I’m fairly sure – which I’ve now lost – that there were exceptions for set-off in something or other in that material. Well, maybe Mr Chesterman can deal with that in reply.

**MR KEENE QC:**

Yes.

**GLAZEBROOK J:**

But of course I think it becomes a bit sort of odd because in fact that asset must have been worth nothing, given the hopelessly insolvent position of MSH2.

**MR KEENE QC:**

Except, just going back to my potential comment to Justice Kós, Mr Hagen did do quite a deal of work on these accounts and made the statements that he made which none of the issues which are being raised now were the subject of cross-examination, there's no question what if it was a fully borrowed funded loan arrangement, but again the evidence is what it is and we can't take it much further.

The last comment I'd like to make before passing over to my learned junior is that Mr Chesterman was asked where there any other differences between the New Zealand and UK regimes and he said that they were quite alike. A point should be made that in New Zealand the time to look at these things is the date of liquidation. In the UK the answer is that it is the time of the transaction. So whatever may have happened going backwards and forwards within those, the difference between those times, would give a different answer. So there's not that much similar to our law.

So unless there's any other further matters which you'd like to ask me, I'll pass over to my …

**GLAZEBROOK J:**

Thank you, Mr Keene. Ms Van.

**MS VAN:**

Your Honours, the next part of these submissions are intended to address the implications which arise out of an acceptance of the test that is being contended for by the appellant. These are covered in summary in our written submissions at paragraph 3.5 and further expanded on from paragraphs 8.21 through 8.26 of the respondents' submissions.

Both parties in this appeal, Your Honours, have relied on the law reforms that have occurred in the parliamentary materials that are in front of this Court, which have been produced, from about 1989 onwards, starting from the Law Commission's report number 9. The purpose of the reform is not contested and is accepted by both parties as having a common purpose of simplifying the liquidation regime and focusing the test on the effect of the transaction rather than having the focus on the intention to prefer a particular creditor. This particular theme is carried through in various subsequent amendments and is reflected in commentary such as the Insolvency Reform Bill, and a reflection of that is being carried through to other places such as the long title of the Companies Act 1993, which is reproduced in the respondents' submissions in its full text at paragraph 6.1, so I won't read them to you, other than to highlight that the regime as it relates to liquidations at least and the stated intention of Parliament was to provide a straightforward and fair procedure for realising and distributing assets of the insolvent company in the liquidation.

The appellant, my friend has relied on presumptions in relation to statutory interpretation today and in particular in asking this Court to impose this additional test of disadvantage or diminution which is said to arise from common law relies on the presumption that it's a code and that this Court should not read down the common law if it's not expressly set out in the Act. What my friend ignores is the other presumptions which arise where this Court is asked to engage in an exercise in statutory interpretation or construction, one of those presumptions being that the Court shouldn't construct or construe a piece of legislation so as to arrive at an absurd outcome, as Justice O'Regan spoke of earlier on today.

My submissions will talk to three key points. The first to highlight the reason as to why there is to be, why simplicity in the regime should be upheld and why it will be undermined in the event the appellant's submissions are accepted. The second issue will deal with some of the evidential complications that will arise, further undermining the simplicity of the test and

also the cost-effectiveness and time-effectiveness of the liquidation regime. And the third point I'll touch on is some of the outcomes that could be arrived at if we accept what my friend is contending for today.

The simplicity of the regime is reflected in various places in the legislation but is also actually reflected in how voidable transactions are pursued by a liquidator. It's intended to be simple to ensure that it's a cost-effective, a time-effective process so as not to diminish any fruits from a recovery action. That promotes collective collection and realisation for the benefit of all unsecured creditors and it's not to be undermined, it shouldn't be undermined quickly in my submission, Your Honours, and what we are likely to see if we accept the test that has been contended for is a process which is going to result in a whole bunch of evidential issues being raised in the context of what is supposed to be a summary process in the first instance where discovery is not even contemplated. This case is a demonstration of some of those issues that can arise. You can see from the materials in front of this Court that the parties were embroiled in skirmishes over discovery from about 2013 through to 2016 and that is reflected in the various judgments that have been issued in the High Court, firstly by Associate Judge Bell, secondly on review by Justice Downs and I believe Associate Judge Sargisson was somewhere in the mix as well in that period, so three years of discovery skirmishes which could have been avoided altogether and is something that my friend says is unlikely to arise if we accept the test that he is contending that we should bring back into how we should apply section 292(2)(b). But an example around evidential complications might highlight why discovery or other such processes are likely to become more common if we adopt the test that's being contended for.

One of the issues which Your Honour Justice O'Regan raised with my friend early on today is this idea that what happens in a situation where you deposit a cheque and at the same time another cheque is written out and how on earth are you supposed to know who gets paid out first, and actually why does it matter which, how is a creditor meant to control that process at all. That is one of the evidential issues that highlights why there will be issues for liquidators in pursuing action if we impose the test that my friend is contending

for, because it will be critical how the source of funds arise from which payments are made. Another example which could be given on the facts of this case, what happens when you've got a deposit of funds into an overdrawn account, for example, say from a receivable that the company was entitled to collect and simultaneously payment is made out to a bunch of different parties, but actually the bank overdraft was there available anyway, how do you separate out that process and how do you trace those transactions through. In my submission, Your Honours, that process will create significant difficulties for liquidators and it's not something that is beyond the realms of reality as my friend would submit. In fact I think it would be my submission that in almost every situation liquidators would have to engage in an exercise in tracing and it would be almost impossible I think in some instances to be able to trace exactly the source of – trace through to the exact source of funds which has been utilised to pay out a particular creditor, particularly where you've got co-mingled funds in an account.

An ancillary issue related to the evidential matters that I've just discussed is the potential back door defences that could be run by creditors in a voidable action by a liquidator. So at the moment we've got a regime where there is a statutory defence, which is set out at 2963. We've also got a running account defence, which is set out at section 292(4)(b). Those were the only legislated defences available to creditors. If we adopt the position that my friend is contending for we may well find ourselves in a situation where the focus of creditors will not be on raising defences under the various provisions which have, in fact, been legislated for, but we end up with people trying to shoehorn defences into 292(2)(b) because there is this ability to put the liquidator to proof in relation to the source of funds and whether there's been a diminution of assets so as to prove the disadvantage.

What we've got at 292(2)(b) Your Honours is a bright line test which is certain and easy to apply. Allowing creditors to raise a further defence under that provision because they have to, because the liquidator has to demonstrate that there's been a diminution of assets and prove the source of funds from which payment was made, could not have been intended by the legislature.

The last point that I'd like to address with you today, Your Honours, I'll take you through the example situation chart that my friend handed up today, which I think was provided titled "Annexure B". He's got two examples in that table. The first one is listed at situation 1, so this is the situation where you've got borrowed funds but they're being paid by the third party direct to a creditor to discharge a debt of the insolvent company, and my friend would say in this situation there's no insolvent transaction because the requisite diminution has not been proven because the assets of the company have not been affected.

At example 4 he raises the example of where an insolvent company borrows funds, and the funds come through the company first before being paid out to a third party creditor, and in that situation his conclusion would be that it's voidable whether on his, on the test that's been proposed, on the test that my friend is proposing to bring back into New Zealand law, or asking this Court to bring back into the New Zealand law.

In my submission, Your Honours, there's no real reason why there should be a distinction on those two sets of facts. If you are borrowing the funds the assumption is that you've got an entitlement to draw down on those funds, whether they be paid direct by the lender, or whether the funds first get paid into your account, then get paid out. There's a case in one of the bundles that you've got in front of you today, Your Honours, *Nangeela*, and in that case the Court made a finding that funds that were paid out from a solicitor's trust account were paid out by the solicitor as agent of the company, and that's precisely what is going on I think when you've got a third party who's paying out at the direction of the insolvent company, and that's the only distinction, but it still makes it a payment by the company and enables there to be a finding that there's been a diminution of assets.

**KÓS J:**
That was a situation of agency, which doesn't apply in the case of a bank I think.

**MS VAN:**

The situation that you’re in when you’ve got funds that are being directed to be paid out to a third party lender is that the third party lender is paying out at your request, and in my submission Your Honour, that is in the nature of that agency arrangement.

As I've already said there is a presumption against construction or interpretation of a legislative provision in a manner that results in absurd outcomes and in my submission, Your Honours, adopting what has been contended for as the disadvantage test will take us right back to where we were back in 1989 and in fact will undermine the whole regime.

So if we, an example, or a hypothetical might assist this Court. If we imagine a company owes 10 creditors $110, and asks to borrow $99, the lender may or may not know why that money is being borrowed, but this is not an uncommon situation in New Zealand. Nine of those 10 creditors get paid 100 cents in the dollar and the 10th creditor gets paid nothing, and then the company subsequently goes into liquidation. If we accept that loans fall outside the scope of 292 because they don’t diminish –

**GLAZEBROOK J:**

Well, I don’t think that’s now the argument. The argument seems to be it’s only if it goes directly from the third party. I mean, I can understand why you're making this submission because I have actually understood the argument to be is you're saying that it seems now that it’s only if it’s an overdraft or goes through the third party, and I think you made the point that why should there be a difference between those two and I’m not sure that we got an answer from Mr Chesterman on that, apart from one’s a diminution and one’s not, which didn’t help very much, personally.

**MS VAN:**

Yes. Well, if we accept for the moment and for the purposes of these submissions that the third party payment would be caught as a payment by the company and it doesn’t diminish the assets of the company, the result

would be that liquidators stepping in would not have the ability to claw back the payments from the nine who received the 100 cents in the dollar in order to equalise the position, and that's precisely what 292 intended to achieve. My friend has made the submission today that the policy underpinning the whole of this regime is to prevent diminishment of assets. That misunderstands the policy reason underpinning the regime, which has been clearly stated in a number of places as being equality, and that is what is the focus of 292. *Heath and Whale* makes the point that you can be in a situation where you're looking at a particular type of transaction that you want to allow a creditor to bring back into the mix, being a transaction that undervalues. So in that situation the policy reason would be seen as giving the liquidator an ability to supplement the asset pool of the company by clawing back an asset which was given away for no consideration. And there's a different thinking behind why you allow those transactions to be clawed back, it's because it has squarely diminished the net asset position of the company, whereas in a situation of a preference you can be in situations where you don't in fact affect the net asset position of the company at all but there has in fact been a preferential effect by virtue of a payment out to one creditor at the expense of other. And the diminishment that we are really interested in is the diminishment of what one creditor could have received over the other, so it's the differential between what the creditors in the pool, in the liquidation, have received as against one another.

One of the key reasons why this change or this test would be undesirable in New Zealand was explained by Her Honour Justice Winkelmann in the Court of Appeal decision at, I believe, paragraph 135, and in that paragraph what she said was, "You don't want to allow this sort of behaviour to occur because it encourages sharp practices of directors of shareholders, of those people in the know," and that's the mischief which we're trying to prevent. It's not just those people in the know but opening the door to the ability for people to argue that there's no diminution and allowing this type of transaction to fall outside the purview of 292 would result, I think, in a situation where directors, shareholders and creditors, friendly creditors, it would allow them to structure their affairs in such a way so as to avoid the scope of 292. It would

also allow directors to pay out those creditors that they've given personal guarantees to ahead of others.

In my submission, Your Honour, adopting this common law test, which my friend is asking this Court to do today, is taking a backwards step. As Parliament pointed out in the Law Reform Report No. 9, one of the key reasons for the change was because the regime as it stood at the time allowed for a situation where people could be preferred, despite the fact that insolvency law was supposed to prevent that outcome altogether, and in my submission, Your Honours, opening the door to this test will land us precisely back in that position that we were in some nearly 20 years ago.

Unless Your Honours have got any further questions?

**GLAZEBROOK J:**
Thank you very much, Ms Van. Mr Keene, is that the submissions?

**MR KEENE QC:**
That's our case.

**GLAZEBROOK J:**
Thank you very much. Mr Chesterman in reply. And can I note just strictly in reply and not a repetition of what we've heard.

**MR CHESTERMAN:**
Thank you for that reminder, Your Honour. Your Honour was enquiring about the passage about the right of set-off. The one that I located was at volume 4, tab 8, and it's Goode's Principles, and it's not referring to –

**GLAZEBROOK J:**
No, it's a set-off the other way.

**MR CHESTERMAN:**
Yes, so that's the reference.

My learned friend, Ms Van, referred to discovery skirmishes and that is an example put forward of why this rule would be a bad thing. This case was unique. Those discovery skirmishes had a lot to do with the fact that Robt. Jones was alleging that this entire transaction was contrived, it was a $4 million licence that was payable over four months to basically do something you don’t need a licence to do. Then it turned out the licence wasn’t even owned by NCI but MSH2 too and then it was sold for $10,000. There was a lot of background information which suggested that this was not a valid transaction at all and that's why those discovery skirmishes existed and they are probably relatively uncommon.

In terms of my friend also mentioned backdoor defences. My submission is that these are always going to happen for those creditors that seek them out. One example which I might go so bravely as to say was a backdoor defence but has been given legitimacy is a separate deed entered between the third party and the creditor, and there’s an example in the authorities, *Grant v Il Forno* [2014] NZHC 1416, that was Justice Gilbert, it’s at volume 2, tab 12, and at paragraph 16 of that judgment where he talks about the fact that the third party entered a separate deed with the creditor and therefore owed the obligation independently of the company. He accepted the whole arrangement was designed to protect Il Forno from the inevitable clawback by a liquidator. So there’s an example of what happens anyway, and my submission is that in any system you have you're going to have people who are going to try and skirt the system.

Those are the reply submissions.

**GLAZEBROOK J:**
Thank you very much. We’ll take time to consider and deliver a judgment in due course. Thank you counsel for your submissions.

**COURT ADJOURNS: 3.58 PM**