Supreme Court of New Zealand
Te Kōti Mana Nui

7 AUGUST 2017

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DAVID BROWNE CONTRACTORS LIMITED AND DAVID BROWNE MECHANICAL LIMITED v DAVID ROSS PETTERSON AS LIQUIDATOR OF POLYETHYLENE PIPE SYSTEMS LIMITED (IN LIQUIDATION)

(SC 57/2016) [2017] NZSC 116

PRESS SUMMARY

This summary is provided to assist in the understanding of the Court's judgment. It does not comprise part of the reasons for that judgment. The full judgment with reasons is the only authoritative document. The full text of the judgment and reasons can be found at Judicial Decisions of Public Interest www.courtsofnz.govt.nz

The issue in this appeal was whether the appellants, David Browne Contractors Ltd (Contractors) and David Browne Mechanical Ltd (Mechanical), should have been ordered to repay sums received from a related company, Polyethylene Pipe Systems Ltd (Polyethylene) in 2008.

At the time Polyethylene's directors (Mr and Mrs Browne) resolved to make the payments to Contractors and Mechanical, Polyethylene was facing a claim for losses arising from allegedly faulty welding it had undertaken for McConnell Dowell Constructors Ltd (McConnell Dowell).

The main question for the Court was whether the claim brought by McConnell Dowell should have been considered a "due debt" for the purposes of s 292(2)(a) of the Companies Act 1993. Under s 292, a transaction is deemed to be an insolvent transaction, and therefore voidable, if, among other things, it is entered into at a time when a company is unable to pay its due debts.

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The Supreme Court has unanimously upheld the repayment order made by the Court of Appeal for the reasons set out below.

Contractors and Mechanical, are, with Polyethylene, part of a group of some 20 companies operated by Mr Browne. In March 2007 Polyethylene entered into a subcontract agreement with McConnell Dowell to weld polyethylene pipes to be laid on the seabed in Lyttelton Harbour. Two of the welds failed during the installation process and a third was identified as defective.

McConnell Dowell informed Polyethylene on 8 May 2008 that it intended to seek recovery of its costs due to the failures in accordance with the indemnity provisions of the subcontract.

In June 2008 Polyethylene's directors resolved to repay unsecured advances from Contractors and Mechanical totalling over $900,000 and also to repay a further debt owed to Mr Browne. It was also resolved that Polyethylene would enter into a general security agreement (the GSA) with Mr Browne to secure $450,000 to fund its ongoing operations.

The directors signed a resolution to the above effect and also signed a solvency certificate dated 1 July 2008. The contingent liability to McConnell Dowell was addressed by stating that the claim was disputed, would be offset by counterclaims for extras and variations and, in any event, would be covered by McConnell Dowell's insurers.

The GSA was executed on 28 July 2008 and the loans were repaid on 2 September 2008. The repayments were made less than a week after McConnell Dowell had written to Polyethylene with a detailed breakdown of the losses it claimed as a result of first weld failure. Those totalled over $2.5m.

McConnell Dowell issued a notice of adjudication under the Construction Contracts Act 2002 on 19 January 2009 and succeeded in its claim against Polyethylene on 20 July 2009. The recoverable losses were set at $2,965,334 plus costs of $31,590.

Mr Browne responded on 29 July 2009 by placing Polyethylene into receivership under the GSA. Polyethylene was then put into liquidation on 5 October 2009 on the application of McConnell Dowell, with Mr Petterson being appointed as liquidator.

On 4 April 2013, Mr Petterson served notices on Contractors, Mechanical and Mr Browne seeking to set aside the payments made to them by Polyethylene on 2 September 2008 on the basis that they were voidable as insolvent transactions under s 292 of the Companies Act 1993.

Mr Browne objected to this notice on 2 May 2013. Contractors and Mechanical did not respond because the accountants who received the notices did not pass them on to Mr Browne. Accordingly, the transactions involving Contractors and Mechanical were automatically set

aside 20 working days after the notices were served under s 294 of the Companies Act.

Mr Petterson brought proceedings in the High Court against Contractors, Mechanical and Mr Browne for an order requiring repayment. He also applied for the GSA to be set aside under s 293 or 299 of the Companies Act. The Associate Judge held that it would not be just and equitable to order that the GSA be set aside as, at the time of the transaction, the claim from McConnell Dowell was not a due debt and therefore Polyethylene was solvent. As to Contractors and Mechanical, the Associate Judge held that there is a general discretion under s 295 of the Companies Act to decline recovery to a liquidator and opted to exercise this discretion.

The Court of Appeal overturned that decision. It ordered that the GSA be set aside and that Contractors and Mechanical repay the amounts paid to them on 2 September 2008.

Leave to appeal to this Court was granted to Contractors and Mechanical on whether the orders for repayment ought to have been made against them. The application for leave to appeal by Mr Browne relating to the setting aside of the GSA and the repayment of certain amounts paid to him was dismissed.

The Supreme Court has unanimously dismissed the appeal. It has held that, if a reasonable and prudent business person would be satisfied that there is sufficient certainty that a claim will become a legally due debt at a temporally proximate point, then it will be a due debt for the purposes of s 292(2)(a). There was such sufficient certainty in the case of the McConnell Dowell claim.

Expert reports available to the directors (including Mr Browne) said that the welding was at the least suspect and that the welds had failed at less than the contractually specified capacity. There was also a significant risk that there would be no insurance cover. Further, the financial position of Polyethylene was such that, even if the McConnell Dowell claim was ultimately assessed at a quarter of the figure set out in relation to the first weld failure, Polyethylene would still not have been able to pay its due debts at the time of the payments to Contractors and Mechanical in September 2008.

There were no defences under s 296(3) or otherwise. In this regard Mr Browne's knowledge and actions must be attributed to Contractors and Mechanical. There were no reasonable grounds for believing Polyethylene was solvent at the time of the transactions. Further, as the transactions were entered into with the purpose of avoiding the McConnell Dowell claim, Contractors and Mechanical did not act in good faith. Given these conclusions, even had there been a residual discretion under s 295 not to order repayment, it would not have been exercised.

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