IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2014-404-1314
[2015] NZHC 3121

UNDER	the Companies Act 1993
IN THE MATTER	of Action Media Limited (In Liqudiation)
BETWEEN	ACTION MEDIA LIMITED (IN LIQUIDATION) First Plaintiff
AND	HENRY DAVID LEVIN AND VIVIEN JUDITH MADSEN-RIES AS LIQUIDATORS OF ACTION MEDIA LIMITED (IN LIQUIDATION) Second Plaintiffs
AND	SEAN WESLEY MITCHELL First Defendant
AND	FARRY & CO TRUSTEES LIMITED Second Defendant

Hearing:	20 November 2015
Appearances:	P Murray and P Shackleton for the Plaintiffs P R Cogswell for the Defendants
Judgment:	9 December 2015

JUDGMENT OF THOMAS J

This judgment was delivered by me on 9 December 2015 at 1.00 pm pursuant to Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Date:………………………….

Solicitors:
Meredith Connell, Auckland.
Cogswell Law, Auckland.

ACTION MEDIA LIMITED (IN LIQUIDATION) v LEVIN AND MADSEN-RIES AS LIQUIDATORS OF ACTION MEDIA LIMITED (IN LIQUIDATION) [2015] NZHC 3121 [9 December 2015]

[1] The first plaintiff, Action Media Ltd (in liquidation) (the Company), was incorporated in 2006. It carried on business as a publisher. It ceased trading on 4 May 2010 and was placed into liquidation by special resolution of its shareholders the same day. The second plaintiffs are the liquidators of the Company (the Liquidators).

[2] The first defendant, Sean Mitchell, was a director of the Company and its sole director from 3 January 2007. Together with the second defendant, Farry & Co Trustees Ltd, which is a solicitor's trustee company, he jointly held shares in the Company.

[3] Unsecured creditors' claims in the liquidation total $1,172,802.93. There are five creditors, the Inland Revenue (the IRD) being by far the largest creditor. All other creditors are related in some way to the Company.

[4] The amounts owed to the IRD include sums for PAYE, goods and services tax (GST), KiwiSaver employee deductions, KiwiSaver employer contributions, student loan employer deductions and interest and penalties.

[5] The Liquidators say that the Company was unable to pay its due debts from at least 31 July 2007 and was balance sheet insolvent from at least 31 March 2008.

[6] The Company pleads three causes of action, in the alternative, against Mr Mitchell, in respect of recovery of remuneration and other benefits paid to a director, under s 161(5) of the Companies Act 1993 (the Act); recovery of distribution paid to a shareholder under s 56(1) and/or s 56(2) of the Act.

[7] The Liquidators claim that Mr Mitchell, as a director of the Company, breached his duties pursuant to ss 131, 133, 134, 135, 136 and 137 of the Act, and failed to keep adequate accounting records and prepare financial statements in accordance with the obligations set out under s 194 of the Act and s 10 of the Financial Reporting Act 1993. They seek to recover the Company's loss in

compensation. The Liquidators then claim against both defendants seeking to set aside insolvent transactions pursuant to ss 294 and 295 of the Act.

[8] The defendants neither admit nor deny the debt owed to the IRD. The defence disputes some debts, claiming that certain creditors have not been included. Mr Mitchell denies the allegations against him and in particular, as is relevant to this decision, pleads:

> In October 2009, the IRD issued a statutory demand. The IRD met with the sole director of the company and reviewed its trading history and prospects and agreed that the company was able to trade on, was able to repay the arrears and was able to meet its current taxes going forward. As a result of the investigation, the IRD specifically agreed an arrangement for the payment of tax arrears in order to allow the company to trade on. The IRD recognised that the company had the ability to meets its taxes going forward and to repay the arrears, hence the arrangement entered into.

Interlocutory application

[9] The defendants applied for orders:

(a) striking out the sixth cause of action;

(b) seeking particular discovery against the plaintiffs;

(c) seeking directions under s 286 of the Act; and

(d) seeking directions regarding Mr Mitchell's discovery.

[10] Shortly before the hearing, the defence advised that the strike out application was not to be proceeded with.

Orders seeking particular discovery against the plaintiffs

[11] The defence seeks particular discovery pursuant to r 8.19 of the High Court Rules (Rules) on the basis that the documents sought are relevant and discoverable and the plaintiffs have refused to provide those documents by way of additional discovery.

[12] The documents fall into three categories as follows:

(a) all notices pursuant to s 261 of the Act issued by the Liquidators;

(b) all correspondence between the Liquidators and the IRD relating to this proceeding; the liquidation of the Company; Mr Mitchell's application for leave to remain a director of Techday Ltd; the consideration of the creditors' compromises and any other matter touching on the issues in the claim; and

(c) unredacted copies of documents LIQ.09.0073 to LIQ.09.00110 from the plaintiffs' supplementary discovery.

Relevant law

[13] The enquiry is whether there are grounds for belief that a party is, or has been, in control of documents which should have been discovered.

[14] The defendants' case is that control in this context includes the ability to require the discovery of documents by another party. Specific to this case, this includes the ability to require the production of documents pursuant to the Liquidators' powers under s 261 of the Act. The applicants say that the Liquidators have the power to compel the release of correspondence involving the IRD and the IRD case notes.

[15] Rule 8.19 of the Rules provides the Court may make an order for particular discovery after the proceeding has commenced where:

> [I]t appears to a Judge, from evidence or from the nature or circumstances of the case or from any document filed in the proceeding, that there are grounds for believing that a party has not discovered 1 or more documents or a group of documents that should have been discovered …

[16] The decision of *Robert v Foxton Equities Ltd* succinctly summarises the relevant principles.[1]

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1 *Robert v Foxton Equities Ltd* [2014] NZHC 726 at [8].

> The following general principles may be taken from decisions of this Court in *ANZ National Bank Ltd v Tower Insurance Ltd* and *Southland Building Society v Barlow Justice Ltd*:[2]
>
> a. A document should be discovered if it is relevant to matters which will actually be in issue before the Court.
>
> b. Relevance is determined by the pleadings.
>
> c. On an application for particular discovery under r 8.19, there must be prima facie evidence that the document exists and is in the party's control (although the applicant need not prove that the document actually exists).

[17] In determining relevance, it is the case of the party seeking discovery which must be assumed to be true rather than that of the party from which discovery is sought.[3]

[18] Rule 1.3(1) provides:

> **1.3 Interpretation**
>
> **control**, in relation to a document, means—
>
> (a) possession of the document; or
>
> (b) a right to possess the document; or
>
> (c) a right, otherwise than under these rules, to inspect or copy the document

[19] The meaning of control in this context was considered in the case of *ISAC (NZ) Ltd v Managh* where, in the context of ss 261(1) and 266(1) of the Act, Gendall AJ (as he then was) said:[4]

> [29] On this, in my view a right to request delivery of documents under s 261 and a right to apply to the Court pursuant to s 266 fall short of the definition of "a presently enforceable legal right" to possession of the documents in question. If, however, a liquidator did succeed in obtaining from the Court a s 266 order then it is clear he or she would at that point have a legally enforceable right. But that is not the case here. And, this is a different situation as I see it from cases where for example the Courts have held that a document is within the power of a party because it is held by that party's solicitors or accountants.

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2 *ANZ National Bank Ltd v Tower Insurance Ltd* HC Auckland CIV-2008-404-7271, 1 September 2009 at [18]–[24] and *Southland Building Society v Barlow Justice Ltd* [2013] NZHC 1125 at [12]–[14].

3 *Kawarau Village Holdings Ltd v Yuen* [2015] NZHC 1379 at 38.

4 *ISAC (NZ) Ltd v Managh* [2012] NZHC 1911.

> [30] In addition, importantly in my view, it cannot be the case that an applicant can force a liquidator, in defending claims against him or her, to expend time and money on speculative pursuits of documents, the need and relevance of which may be seriously in question.
>
> [31] In summary, what the applicant contends here is that the respondent has a right to apply for a court order to obtain third party documents under s 266 Companies Act 1993, and that must equal a power of enforceable legal right over those documents equating to control. I reject this contention however.

[20] I agree generally with that analysis, which I consider in more detail below.

Section 261 notices

[21] The defendants say that the s 261 notices are relevant because they relate specifically to enquiries made by the Liquidators about the conduct of the Company and so could be of material relevance to their defences. They point out that the Liquidators have already discovered two s 261 notices (s 261 Notices) and, on that basis, in Mr Cogswell's submission, all s 261 notices should be discovered as the Liquidators should not be able to "cherry pick" some notices but not others.

[22] Mr Cogswell submits that the Liquidators are in control of the s 261 notices as they issued them and, accordingly, they should all be discovered.

[23] Mr Cogswell refers to the s 261 Notices which the Liquidators acknowledged are relevant and discovered. The first Notice, in July 2010, related to whether money had been received from the Company and the second Notice, in August 2012, asked whether the second defendant had received Company funds as trustee. It was after the response that the second defendant was joined to the proceedings. Mr Cogswell accepts that the s 261 Notices fall into the category of relevance but, in his submission, there might also be others issued to other creditors which touch on matters relevant to the defence. Mr Cogswell points out that, as the defendants do not know to whom the s 261 notices have been issued, they are unable to identify them. Their relevance, in Mr Cogswell's submission, is that they are enquiries about the way in which the Company operated and how Mr Mitchell discharged his obligations as a director.

[24] The Liquidators say that all relevant documents, including all relevant s 261 notices, have been discovered. As Mr Shackleton points out, s 261 notices are simply requests for information. It is the responses to them which are more likely to be relevant to these proceedings and there is no suggestion that relevant responses have not been discovered. The Liquidators also point to the time and cost of checking the files to ensure that all s 261 notices have been discovered.

[25] The way in which the request is made – that is, that the s 261 notices might raise an issue which might lead to further enquiry – emphasises the difficulty with the application and whether this is indeed simply a fishing expedition, as the Liquidators say.

[26] It is important to focus on the proceedings and the issues therein. These proceedings are not an enquiry into how the liquidation of the Company has been carried out.

[27] The Liquidators have said that all relevant s 261 notices have been discovered. The fact that some have been discovered emphasises compliance with discovery obligations. Simply because some s 261 Notices have been discovered does not mean that all s 261 notices are relevant.

Correspondence

[28] The correspondence requested by the defendants includes correspondence relating to Mr Mitchell's application for leave to remain a director of Techday Ltd and the consideration of the creditors' compromises. It seems that the creditors' compromises refer to two different compromises reached with the IRD; the first relating to the Company and the second relating to Mr Mitchell's personal compromise with the IRD concerning his personal debt.

[29] The defendants refer to the efforts they have made to obtain copies of these documents direct from the IRD, including making a request under the Official Information Act 1982. The IRD effectively has refused to provide the information sought.

[30] Section 261 of the Act relevantly provides:

261 Power to obtain documents and information

(1) A liquidator may, from time to time, by notice in writing, require a director or shareholder of the company or any other person to deliver to the liquidator such books, records, or documents of the company in that person's possession or under that person's control as the liquidator requires.

(2) A liquidator may, from time to time, by notice in writing require—

(a) a director or former director of the company; or

(b) a shareholder of the company; or

(c) a person who was involved in the promotion or formation of the company; or

(d) a person who is, or has been, an employee of the company; or

(e) a receiver, accountant, auditor, bank officer, or other person having knowledge of the affairs of the company; or

(f) a person who is acting or who has at any time acted as a solicitor for the company—

to do any of the things specified in subsection (3).

(3) A person referred to in subsection (2) may be required—

(a) to attend on the liquidator at such reasonable time or times and at such place as may be specified in the notice:

(b) to provide the liquidator with such information about the business, accounts, or affairs of the company as the liquidator requests:

(c) to be examined on oath or affirmation by the liquidator or by a barrister or solicitor acting on behalf of the liquidator on any matter relating to the business, accounts, or affairs of the company:

(d) to assist in the liquidation to the best of the person's ability.

...

(7) Nothing in this section limits or affects section 260.

[31] Not only is someone who fails to comply with a s 261 notice liable to conviction and penalty but also the Court can order compliance pursuant to s 266.

[32] In this case, the Liquidators clearly considered the compromise reached with the Company in respect of its liabilities to be relevant. On 4 May 2015, the Liquidators wrote to the IRD as follows:

> Notice to Provide Records to Liquidator
>
> (Section 261 of the Companies Act 1993)
>
> Action Media Limited (In Liquidation) ("the Company") was placed into liquidation on 4 May 2010 by special resolution of shareholders. …
>
> In accordance with Section 261 of the Companies Act 1993 we require you to deliver:
>
> - Copies of all correspondence and files relating to the Company's overdue tax debt after July 2007
> - A copy of the Statutory Demand served on the Company and confirmation of the date the demand was served on the Company
> - Details of any payment plans/proposals entered into between the Company and Inland Revenue.
>
> Please provide this information by Friday 22 May 2015.
>
> Please note that no lien can be asserted against the liquidators.
>
> Section 261(6A) of the Companies Act 1993 states that a person who fails to comply with a notice given under Section 261 of the Companies Act 1993 is liable on conviction to a fine not exceeding $50,000 or to imprisonment for a term not exceeding 2 years.
>
> Section 266 of the Companies Act provides that a person who fails to comply with this notice may, on the application of the Liquidator, be ordered by the Court to comply.

[33] The notice specifically required all correspondence and files relating to overdue tax, debts and details of any payment plans or proposals entered into between the Company and the IRD.

[34] An IRD employee requested further detail about the request and correspondence between the IRD and the Liquidators ensued. Eventually, by email dated 3 September 2015, the IRD responded saying:

> I attach the screen records of the two correspondences requested. I am unable to locate the others requested.

[35] Apparently, the Liquidators took no further action. This is despite the letter of 4 May 2015, making it clear that it was an offence not to comply and that the Court could order compliance.

[36] The information about the compromise reached between the IRD and the Company on outstanding liabilities to the IRD is clearly central to these proceedings. The IRD is not only the largest creditor but is also the only creditor who is truly independent of the Company. I accept Mr Cogswell's submissions that the IRD will reap the benefits of these proceedings by obtaining payment of the sums outstanding to it.

[37] Notwithstanding my observations in connection with the case of *ISAC (NZ) Ltd* above, this case is clearly in a different category. This is not a situation where the defendants are seeking to force a liquidator to spend time and money on speculative pursuit of documents, the need and relevance of which may be seriously in question. This is a situation where the Liquidators have already requested the documents and the IRD has purported, but clearly failed, to comply with the Notice. It is inconceivable, given the IRD's statutory obligations, that it has not retained copies of the correspondence. The request from the Liquidators falls clearly within s 261, and ss 261(2) and (3) are relevant. Arguably, the Liquidators are under a duty to pursue the IRD for the information given its role in these proceedings.

[38] The correspondence must be relevant to the Liquidators' assessment of the claim against Mr Mitchell. This is different from the case of *ISAC (NZ) Ltd* because the Liquidators have already initiated the request for the documents.

[39] The question is, in accordance with the definition of "control" under r 1.3(1) of the Rules, whether the Liquidators have "a right to possess the document". It is clear that, having made the request, the Liquidators have the power to seek enforcement of compliance with the notice thus a right to possess the correspondence. In the circumstances of this case, the Liquidators should pursue the request with the IRD and seek enforcement of any non-compliance. Even if I am wrong, it would be highly likely that the defendants would be successful in an application for non-party discovery. They should not be put to that cost and expense

and, given this decision, I would expect that such an application would not be required.

Techday Ltd directorship

[40] In Mr Cogswell's submission, the information as to Mr Mitchell's suitability to be a director of Techday Ltd is directly relevant. The background to this matter is that there was a related proceeding, being an application under s 382 of the Act, for leave for Mr Mitchell to continue as a director of Techday Ltd. The other party to the application was the Registrar of Companies (Registrar) who initially opposed the application. A senior enforcement officer at the IRD provided an affidavit in support of that opposition. Ultimately, the Registrar consented to the application with the effect that Mr Mitchell could continue to be a director of Techday Ltd. That being the case, in Mr Cogswell's submission, the Registrar must have satisfied himself that Mr Mitchell was a proper person to be a company director. That is a relevant consideration in this case, in his submission, when the Court comes to exercise its discretion under s 301 of the Act.

[41] Mr Cogswell says that the affidavit provided on behalf of the IRD in those proceedings contained correspondence between the IRD and Mr Mitchell including, potentially, relevant correspondence of which Mr Mitchell does not have copies. In his submission, the affidavit in those proceedings confirms the documents exist and the information is relevant and within the Liquidators' power to obtain.

[42] However, the power of the Liquidators pursuant to s 261 of the Act relates to the production of documents of the **Company** or information about the Company.

[43] Correspondence between the IRD and Mr Mitchell about Mr Mitchell's personal compromise with the IRD is not something the Liquidators would be able to obtain pursuant to a s 261 request. The agreement pleaded in the second statement of defence is an agreement between the Company and the IRD and Mr Mitchell's personal tax situation is irrelevant.

[44] The argument is advanced on the basis that the fact the IRD might have considered Mr Mitchell fit to be a director of Techday Ltd is relevant to the general

question of his fitness as a director. In this regard, however, the IRD opposed Mr Mitchell's continuing to be a director of Techday Ltd and it was the Registrar who eventually consented.

[45] This correspondence is clearly in a different category from that relating to the IRD's compromise with the Company. It is not in the control of the Liquidators and discovery of it cannot be achieved pursuant to the application.

Case notes

[46] The defendants also seek discovery of unredacted copies of the IRD case notes.

[47] The Liquidators point out that the redactions were made by the IRD prior to the documents being provided to the Liquidators. The Liquidators do not hold unredacted copies of the case notes which are internal IRD records and, accordingly, the Liquidators cannot discover them.

[48] Mr Shackleton again refers to the Liquidators' powers under s 261 which permits the Liquidators to compel production of books, records or documents of the Company, that is, the Company's own documents and not the documents of a third party.

[49] Furthermore, although Mr Cogswell refers to discovery obligations generally, submitting that the IRD does not have authority to make redactions from a document which is discovered, documents provided pursuant to the s 261 notice procedure are not covered by those same rules.

[50] The IRD case notes are not documents "of the Company". Furthermore, the Liquidators have discovered documents received from the IRD and it is the IRD who made the redactions.

[51] In those circumstances, I do not accept that the Liquidators could use s 261 to compel production of unredacted case notes.

[52] The Liquidators also make the point that the redactions appear to be the same on every case note and that the one unredacted case note provided suggests that the redactions are immaterial.

Section 286 of the Act

[53] The defendants oppose the continuation of the Liquidators' use of powers under s 261 of the Act by issuing notices to, inter alia, Mr Mitchell.

[54] In Mr Cogswell's submission, the notices are effectively interlocutories and should therefore properly be conducted as such.

[55] There is one s 261 Notice which has been issued to Mr Mitchell which remains outstanding. In Mr Cogswell's submission, there is evidence that the Liquidators are not investigating any further claims and there is therefore no justification for issuing any further notices. Rather, in his submission, it is an abuse of their power.

[56] It seems that the outstanding notice relates to a creditor claim by Acumen Holdings Ltd, a related company. Mr Shackleton points out that the amount claimed is not in dispute but he says some documents provided by Acumen Holdings Ltd do not correspond with the Company's records. Mr Mitchell, as director, was therefore asked to clarify certain points. It is, in Mr Shackleton's submission, a reasonable request to make to a director who will have personal information regarding the issue. The process is not being used, he says, to gain litigation advantage.

[57] Furthermore, the Liquidators seek compensation from Mr Mitchell for the full amount of Acumen Holdings Ltd's claim. If the amount can be reduced by reason of information provided by Mr Mitchell, then that could only be to Mr Mitchell's benefit, says Mr Shackleton.

[58] The only indication given by the Liquidators that they did not intend to take further action related to potential voidable preference claims. There is nothing to prevent the Liquidators from continuing to make proper enquiries. In any event,

simply because the Liquidators might have given an indication to one party, that does not preclude them from acting contrary to that indication.

The first defendant's discovery obligations

[59] Part of Mr Mitchell's discovery includes document AML 5 which is described as "AML tax invoices and receipts from suppliers".

[60] A standard discovery order was made in February 2015 requiring Mr Mitchell to list and provide electronic copies of all relevant documents.

[61] Mr Mitchell now seeks to require the Liquidators to attend his lawyer's office to review the documents on the basis they are "only marginally relevant" and they can require electronic copies of any documents they actually need.

[62] The Liquidators had sought to settle this issue by requesting that Mr Mitchell confirm he did not intend to rely on the documents at trial. If that undertaking were given, then the Liquidators would agree to inspect the documents at counsel's chambers. However, Mr Mitchell is not prepared to provide that confirmation.

[63] Mr Cogswell says that Mr Mitchell cannot make that compromise as the documents are clearly relevant. Instead, he relies on a proportionality approach. The cost of scanning the documents and providing them electronically would be expensive and time consuming. Mr Cogswell refers to r 8.12(3) of the Rules.

[64] I acknowledge there are issues as to proportionality. In saying that, perhaps this could be settled by Mr Mitchell identifying those documents on which he intends to rely and providing scanned copies to the Liquidators. The Rules make it plain that the Court expects counsel to co-operate about matters such as this.[5]

[65] I accept the difficult position in which the Liquidators have been placed – that is, if some or all of the documents are to be relied on then, inevitably, someone representing the Liquidators will have to take time to inspect the documents with a

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5 High Court Rules, r 8.2.

greater level of review than might otherwise be the case. However, they will have to inspect the documents anyway – whether in person or by viewing electronic copies.

[66] In all the circumstances, when the documents in issue are simply the invoices pursuant to which the accounting entries have been made, I accept that their relevance is marginal. I am satisfied that the cost of scanning the documents and providing them electronically would be out of proportion to the materiality of the documents. The application is granted. The Liquidators are to attend at the offices of the first defendant's lawyer, inspect the documents, and then advise which, if any, need to be electronically scanned and provided.

Results

[67] For the reasons given:

(a) The defendants' request for discovery of s 261 notices is declined.

(b) The defendants' request for correspondence relating to the consideration of the creditor's compromise regarding the Company is granted.

(c) The defendants' request for correspondence between the IRD and Mr Mitchell about Mr Mitchell's personal compromise with the IRD is declined.

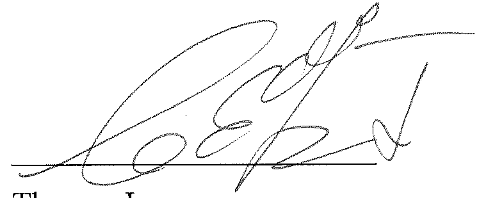
(d) The defendants' request for unredacted copies of the IRD case notes is declined.

(e) The first defendant's application as to the mode of discovery and inspection is granted.

Costs

[68] The plaintiffs seek costs in respect of the strike out application which was not pursued.

[69] Costs can be dealt with by memoranda and will be decided on the papers.



Thomas J