IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV 2013-404-001150
[2013] NZHC 1152

UNDER	the Companies Act 1993
IN THE MATTER OF	an application to terminate the liquidation of Silverdale Developments (2007) Ltd (In Liquidation) and review liquidation costs
BETWEEN	ANTHONY BUNTING AND GARY RAYMOND COOPER Applicants
AND	JOHN BUCHANAN First Respondent
AND	CALLUM MACDONALD Second Respondent

Hearing: 15 May 2013

Appearances: L J Turner for applicants
G P Blanchard for first respondent
D P H Jones QC for second respondent

Judgment: 20 May 2013

JUDGMENT OF ASSOCIATE JUDGE ABBOTT

This judgment was delivered by me on 20 May 2013 at 11.30am,
pursuant to Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Date……

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[1] This case concerns a dispute over the costs of liquidation of Silverdale Developments (2007) Ltd (Silverdale).

[2] The shareholders of Silverdale applied in March 2012 for termination of the liquidation, and for review of the remuneration charged by the liquidators. An order for termination was made, by consent, on 2 May 2013, leaving the dispute over costs still to be determined.

[3] This decision addresses issues over discovery sought by the applicant shareholders ahead of a hearing of their substantive application.

Background

[4] The applicants are shareholders and directors of Silverdale. Silverdale was incorporated to develop a property at 18 David McCathie Place, Silverdale, into several units comprising offices and warehouse space. After completion of the development and on-sale of the units, the shareholders put Silverdale into liquidation. They regarded it as a solvent liquidation. The second respondent was appointed liquidator.

[5] Shortly after taking possession, the purchasers of the units noticed cracking in the concrete floor of the units. They raised this with the applicants but after investigating the parties came to widely differing views over the cause of the cracking and the likely remedial cost.

[6] The purchasers were unaware of the liquidation for a considerable period (they were dealing just with the applicants). When they did learn they lodged a proof of debt with the second respondent, claiming their estimated cost of repair. This led in turn to the second respondent applying to this Court under s 307 of the Companies Act 1993 to determine the quantum of the purchasers' claims.

[7] A further dispute arose between the shareholders and the second respondent over this proceeding. This led to the first respondent being substituted as liquidator.

The first respondent withdrew the second defendant's application. He also rejected the purchasers' claims in the liquidation, taking the view that they needed to be determined in separate proceedings between the company and the purchasers.

[8] The applicants were concerned about the costs of the dispute with the purchasers and wished to take control of Silverdale's defence. They applied for termination of the liquidation. That application was declined.

[9] Prior to the application for termination being determined, the purchasers issued a claim for substantial damages, being the alleged cost of remedying defects in the units. Silverdale, the applicants, and several parties involved in the construction were joined as defendants in that proceeding. The purchasers' claims were eventually settled shortly before trial. Silverdale was not required to pay any amount under that settlement. As a consequence it was left with its sole asset (shares in a company owning an office/warehouse at 16 David McCathie Place valued at about $1.34m).

[10] The applicants take issue with the level of costs charged by both liquidators as a consequence of the drawn-out liquidation. The first respondent claims that the total costs of the liquidation are in the order of $973,000 (inclusive of the second respondent's costs). This includes approximately $362,000 for his fees as liquidator, together with substantial legal and engineering fees. The second respondent has charged costs of approximately $60,000 for his work as liquidator billed up to the time of his replacement, and a further sum of approximately $11,000 billed since.

[11] The applicants accept that reasonable costs are payable, but say that the sums charged are manifestly excessive.

The discovery issues

[12] At the first call of the application on 10 April 2013, the applicants sought discovery of various categories of documents. The first respondent agreed to provide discovery of his diary, electronic records relating to his costs and disbursements, and travel records. I recorded the parties agreement in a minute

dictated in the presence of counsel. The applicants contend that the first respondent has not complied with that agreement, and also say that discovery is needed of physical records from which the electronic time records were entered and of the first respondent's files (including those held by his professional advisors). The first respondent disputes the claim that he has not complied with the earlier agreement, and also challenges the applicants' entitlement to any further discovery.

[13] The applicants have also sought access to the second respondent's files. Those parties have agreed to a process to meet that request.

The first respondent's electronic records

[14] The applicants accept that they have received the first respondent's diaries and travel records but say that they have not received the electronic records in a form that they can access. The first respondent initially refused to supply these records, contending that he was unable to separate the records for this liquidation from other matters. Subsequently it appears that he was able to do so, as he provided the applicants with a flash drive said to contain time records for this liquidation only. The applicants say they have been unable to access all of the information on that flash drive, even with technical assistance, but in any event wish to see the physical records for all work in the period, given recent advice that electronic records were created only recently.

[15] I see no reason, on the material currently before the Court, to question the first respondent's statement that he has complied with this part of the agreement (I will come back to the request for other records). However, I reserve leave to the applicants to seek directions if they continue to have difficulty accessing the information and are unable to obtain information from the first respondent needed to get access.

[16] The second alleged aspect of non-compliance is that the first respondent has not provided copies of other electronic records "such as e-mails and other documents held electronically". The first respondent takes the position that there was no agreement to do so.

[17] I accept the first respondent's submission that there was no agreement to include e-mail in the documents to be discovered. However, I do not rule out the prospect of an order, but it will be for the applicants to make a case for it. Their current request is too broad. If they wish to pursue it (and it may be redundant given the arrangement for access to files to which I will refer shortly), the applicants will need to be more specific about what they are seeking and show how those documents could be relevant to the review of costs.

Additional discovery by the first respondent

[18] The first respondent has informed the applicants that the electronic records were created only comparatively recently. As a consequence the applicants are now also seeking further discovery to allow them to test the veracity of the first respondent's claim that the electronic records are an accurate record of time spent (they argue that the records are an unsupported and inaccurate reconstruction or fabrication):

(a) They have been given access to physical time records that the first respondent says underlie the electronic records, including copies of documents recording time entries for this liquidation only, on a month by month basis. They wish to inspect the originals to assess whether these records were made as work was done or afterwards. This is because an initial inspection of the originals of the first respondent's diaries indicates that the time record entries in them were all written in the same pen whereas various pens were used to record appointments and other entries over the two year period.

(b) They also seek the first respondent's time records for other work being conducted through the same period to assess whether the manner in which the first respondent says that he recorded his work on this liquidation is consistent with the way he recorded his work on other matters.

[19] The applicants also seek discovery of all of the first respondent's liquidation files and the related files of his advisors, to be able to assess the value of the work undertaken. They say that it is necessary for them to inspect those files and be entitled to request copies of documents from them because:

(a) the records that have been disclosed show that almost all of the time recorded by the first respondent was spent reviewing documents and e-mails provided by his advisors; and

(b) they are seeking a review of expenses incurred, and cannot assess whether the expenses are legitimately claimed without access to the files.

[20] Their counsel submitted that it would not be a costly exercise, as the files could be made available as they exist (the applicants do not seek formal listing), and there was no need to separate privileged material as it was only being reviewed by Silverdale's directors.

[21] The first respondent does not oppose discovery of the original physical timesheet records from which the electronic records were compiled, and says that it was only due to an oversight that they were not available for the applicants' inspection with the other records. However, he opposes discovery of his liquidation files and the files of his advisors on three grounds:

(a) Discovery is not usual in originating applications: the agreement made at the first call was by way of exception to that normal rule, and there is no reason to revisit the limited scope of that discovery.

(b) It would be a massive task to prepare them for inspection having regard to the amount of documentation, and a need to extract privileged documents.

(c) Although he had been willing to discuss and come to an agreement over the expenses in the period since the last hearing, that has not

> been possible because the applicants maintain the position that all expenses are disputed. For that reason he maintains his primary position that the Court does not have power to review expenses, and that it would be contrary to basic principle to review the reasonableness of a third party's fees in the absence of that party.

[22] Counsel for the first respondent did not address me specifically on the request for time records for other work, but I understand that request is also opposed.

[23] During the hearing, counsel for the first respondent withdrew the first respondent's opposition to providing files for inspection subject to privileged documents being separated out, and to the costs of preparing the files for inspection being met.

[24] Counsel for the applicants maintained their challenge to the first respondent's entitlement to privilege as against them, but said that in any event the files could be made available for inspection just by counsel in the first place (who could make a decision on what documents the applicants wished to obtain from the files), and any issue over privilege could be addressed when the document was requested. He opposed any order for the applicants to meet the cost of preparing the files for inspection.

Should discovery be ordered?

[25] The first respondent's change of position in the hearing was an appropriate one. The applicants are contesting the value of the work done. It is not possible to address that fairly without knowledge of the work that was undertaken. The Court has the power to make orders for discovery under Part 8 of the High Court Rules. There is no specific provision for discovery in relation to originating applications. Until the recent amendment to the High Court Rules introducing a new discovery regime[1] the Court had a discretion as to whether to order discovery for cases on the swift track. The distinction between standard and swift track cases has been removed by the amendment, and the Court is now required to make an order unless

[1] High Court Amendment Rules (No. 2) 2011.

satisfied that the case can be justly disposed of without any discovery.[2] Unless the Court decides that discovery is not required, the focus is on whether to order standard or tailored discovery.[3]

[26] The agreement reached at the hearing on 10 April, and the proposal for inspection of files rather than formal listing of all documents, are appropriate applications of the approach for tailored discovery. I order the first respondent to provide tailored discovery by making his files available for inspection by the applicants and providing them with copies of any documents they may request.

[27] In light of the order just made, there is no need for me to determine the issue as to whether the first respondent was required to provide email correspondence and other electronic documents as part of the agreement reached on 10 April 2013. However, this order is not to be taken as support for the Court's power to review the fees of the first respondent's professional advisors (a matter I will come back to shortly). The issue in this case is the reasonableness of the costs charged in the liquidation. The advisors' files will, however, help to inform the applicants and the Court on the related questions of what advice or services the first respondent sought from the advisors and whether it was reasonable of him to do so.

[28] The first respondent is also to provide the applicants with samples of his time records for other work to allow comparison between the records for this liquidation and for other work. If the parties are unable to agree on the method of sampling, leave is reserved to the applicants to seek a telephone conference to resolve the point.

Does the first respondent have a separate claim to privilege?

[29] As I understand their counsel's argument, the applicants say that the first respondent (as liquidator of Silverdale) does not have a claim to privilege separate from Silverdale, so that there is no reason to prevent the applicants, as Silverdale's directors, from viewing all the documents. In the alternative, counsel argued that he

[2] High Court Rules, r 8.5.
[3] R 8.6 – 8.8.

should be permitted to inspect the files and determine what documents were needed in the first place, and the first respondent could raise any claim to privilege in any documents that were requested before the applicants had access to them.

[30] The first respondent may have an entitlement to privilege separate from the company, particularly in relation to the contest between him and the applicants over termination of the liquidation, and the challenge to his costs. It follows that the first respondent must be able to make a claim for privilege, and the applicants must have a corresponding entitlement to challenge that claim, in the usual way (that is, subject to any agreement between the parties, in accordance with the High Court Rules).

[31] Any claim must be assessed on a document by document basis. The starting point must be for the first respondent to identify from his files (and the files of his professional advisors) any material in which a claim for privilege properly lies, and the nature of the privilege. I do not consider it appropriate for counsel to inspect the documents before privileged documents are removed.

How are the costs of this discovery to be met?

[32] In the hearing I discussed with counsel whether it might be appropriate for the applicants (as the party seeking the documents) to meet the costs of discovery of the liquidators' files in the first instance. On further reflection I consider that the proper approach is to treat the costs of the discovery as part of the costs of liquidation, subject to review as part of the substantive application.[4] If the Court accepts that it was appropriate for the first respondent as part of his duties as liquidator to seek and consider advice from professional advisors and to instruct the advisors to carry out the work they undertook, he should be entitled to have those costs met as part of the costs of liquidation. However, if the advice sought, or work undertaken, was not for the proper conduct of the liquidation, but was sought/undertaken in respect of the first respondent's personal position, there may be an argument that the costs of the advice/work are not costs of the liquidation.

[4] See *Fraser Thomas Limited v Springs Town Limited* HC Auckland CIV-2009-404-007829, 20 April 2011 at [46].

[33] Ultimately, the question will be whether it was reasonable for the first respondent, as liquidator, to seek the advice or instruct professional advisors to undertake the work that underlies the fees charged by those advisors. That will need to be determined with knowledge of what advice was sought and it may be necessary to see the advice or instructions to determine whether the time spent considering it or carrying it out was a reasonable cost. The same question arises in relation to the costs of undertaking this discovery. The Court may need to inspect the documents in which privilege has been claimed.

[34] The initial cost to the first respondent will be lessened by production of files. There will be a cost involved in identifying documents for which privilege is claimed, but it seems reasonable that that cost should be recoverable in due course unless the claim is made without proper foundation.

The first respondent's claim for expenses

[35] One of the grounds advanced by the first respondent for not disclosing his files was that expenses incurred in the liquidation are not reviewable (relying on *Re Medforce Healthcare Services Ltd (In Liquidation)* and *Re Roslea Path Ltd (In Liquidation)*).[5] The applicants contend that it is still arguable that expenses can be reviewed, and say that this is an argument for the substantive hearing.

[36] Although the Full Court in both *Re Medforce* and *Re Roslea* did not expand upon the point, there is no doubt that the Court in *Re Medforce* found as a matter of construction of the Act that expenses are not reviewable. The Court in *Re Roslea* merely referred to the statement in *Re Medforce*. I do not need to determine whether it is still open to the applicants to seek review of expenses, particularly where the advisors are not a party to the review, as I consider that the advisors' files should be made available. This will not be done to assess the reasonableness of their fees but rather to assess whether it was reasonable for the liquidator to have instructed them to undertake the work for which the fees were charged.

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[5] *Re Medforce Healthcare Services Ltd (In Liquidation)* [2001] 3 NZLR 145 (HC) at [19]; *Re Roslea Path Ltd (In Liquidation)* [2013] 1 NZLR 207 (HC) at [45].

Discovery by the second respondent

[37] Since the first hearing the second respondent has filed an affidavit to which he has exhibited his timesheets and other material to support the fees he is claiming. In response to a request by the applicants he has offered to make his files available as well on condition that the applicants provide a substantial response as to what aspects (if any) of the second respondent's fees are challenged, and the grounds for any challenge. His counsel makes the point that these fees need to be addressed as a discrete issue, separate to the fees of the first respondent.

[38] The applicants are not seeking the files of the professional advisor engaged by the second respondent. His fees have been challenged and remain unpaid. They are not part of the costs of liquidation being claimed by the respondents.

[39] The parties have discussed a timeframe for provision of the second respondent's files, for inspection by the applicants, and for a response. Counsel for the second respondent asks for timetable orders as discussed, ahead of a further review in a month's time. Counsel for the applicants has agreed to that timetable.

Hearing of substantive application

[40] The respondents seek allocation of a hearing for the substantive application at this point. The applicants say it is premature until their requests for discovery have been met.

[41] When this application first came before the Court on 10 April 2013, the parties agreed that the matter was capable of being heard substantively in August 2013. I see no reason to depart from that position. It seems likely, given the issues raised by the applicants, that cross-examination of deponents will be required and may be extensive. However, even with extensive cross-examination, the substantive hearing should be completed within three days, and that estimate may be reduced once the issues for determination are settled following discovery.

[42] The first respondent has applied for appointment of a costs assessor, and says he would accept the assessor's determination. The applicants oppose such appointment saying that the decision on whether the fees are reasonable is ultimately one for the Court. I have discussed with counsel whether there is any merit in an appointment to establish facts ahead of the substantive hearing. Having heard counsel on the point I am not persuaded that much, if anything, would be gained, and it would add another layer of cost. Counsel for the first respondent has not pursued the application.

[43] I propose allocating a trial date on the basis of what I regard as the maximum time required, and reviewing that estimate at a further mention hearing in a month's time.

Orders

[44] I make the following orders to carry these decisions into effect:

(a) The applicants are to inspect the second respondent's files and advise the second respondent of the documents of which they require copies, and the second respondent is to provide copies of the documents requested, by **29 May 2013**.

(b) The applicants are to respond to the second respondent in writing by 14 June 2013, identifying what aspects of the second defendant's fees are accepted and what aspects (if any) they continue to dispute, and stating the grounds for any dispute(s), by **14 June 2013**.

(c) The first respondent is to make his files and the files of his professional advisers (save for documents for which he claims privilege) available for inspection by the applicants by **29 May 2013**.

(d) The first respondent is to provide the applicants with a schedule of any documents for which he claims privilege, drawn up in accordance with the High Court Rules, by **29 May 2013**.

(e) The applicants are to complete inspection of the first respondent's files and the files of his advisors, and notify the first respondent in writing of any challenge(s) to the claim(s) for privilege, by **14 June 2013**.

(f) The application is to be listed for further mention in the chambers list at **2.15pm on 19 June 2013** to address any issues arising out of this discovery (counsel may file a joint memorandum requesting vacation of the mention hearing if there is no matter needing directions, or if directions can be made by consent). If a joint memorandum is not provided, updating memoranda are to be filed and served by the **applicants by 14 June 2013** and the **respondents by 17 June 2013**.

(g) The applicants are to file and serve any further affidavits in support of their application by **1 July 2013**.

(h) The respondents are to file and serve any further affidavits in opposition by **29 July 2013**.

(i) The Registrar is to allocate 3 days for hearing of the substantive application **commencing at 10am on 26 August 2013**.

(j) The estimate of time for hearing will be reviewed, and any pre-trial directions required will be given, at the mention hearing on 19 June 2013, unless counsel can address them in advance in a joint memorandum.

(k) Any party wishing to have clarification of these orders or to raise any matter not addressed by them may approach the case officer and request a **telephone conference at 9am on 23 May 2013**.

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Associate Judge Abbott