IN THE COURT OF APPEAL OF NEW ZEALAND

CA701/2011
[2012] NZCA 442

BETWEEN	SUSAN NANETTE HERBERT Appellant
AND	NEW ZEALAND GUARDIAN TRUST COMPANY LIMITED & ORS Respondents

Hearing: 18 September 2012

Court: Randerson, Stevens and Miller JJ

Counsel: A Barker for Appellant
B J Upton and B J Steed for Fourth Respondent Westpac New Zealand Limited
No appearance for First, Second, Third, Fifth and Sixth Respondents

Judgment: 27 September 2012 at 11.30 a.m.

JUDGMENT OF THE COURT

A The applications by both parties to adduce further evidence on appeal are granted.

B The appeal is dismissed.

C There is no order for costs.

REASONS OF THE COURT

(Given by Randerson J)

Introduction

[1] The appellant Mrs Herbert and her husband became involved in a property development at Pauanui on the Coromandel Peninsula. The project involved the construction of a golf course, the subdivision of residential land and the sale of

sections and villas to be constructed. The development was described by the Judge in the Court below as a spectacular financial failure.

[2] Five other persons who had joined Mr Herbert in the venture were adjudicated bankrupt. Applications to have Mr and Mrs Herbert adjudicated bankrupt were filed in late 2010. Shortly before the hearing date for these applications, both Mr and Mrs Herbert separately applied for approval of creditors' proposals under s 333 of the Insolvency Act 2006 (the Act). In a judgment delivered on 26 September 2011, Associate Judge Doogue declined both applications.[1] Mrs Herbert now appeals against the Court's refusal to approve her creditors' proposal. No appeal has been brought by Mr Herbert.

[3] Although five creditors appeared in the High Court when the proposals were considered, the only creditor appearing to contest the appeal is the fourth respondent Westpac New Zealand Ltd (Westpac).

[4] Initially, it appeared that the appeal would not be opposed by any creditor. However, that position changed when, on 5 September 2012, Westpac filed an application for leave to adduce further evidence on the appeal and indicated that it would be appearing to oppose the appeal despite earlier advice that it would not do so. This led to a very late application by Mrs Herbert for leave to file further evidence on appeal disputing aspects of the evidence that Westpac sought to advance. This gave rise to several preliminary issues we now address.

Preliminary issues

[5] The first preliminary issue is whether the respective applications for leave to adduce further evidence on appeal ought to be granted. We indicated during the hearing of the appeal that we would grant both applications and we now do so. The further evidence from Westpac was an affidavit from Ms Gellert, a solicitor employed by Westpac's legal advisers, Simpson Grierson. She deposed that Westpac had not received notice of the creditors' meeting as required by s 330 of the Act, to

[1] *Herbert v Allied Nationwide Finance* HC Auckland CIV-2010-404-8294, 26 September 2011.

be held in order to consider the creditors' proposals. In consequence, Westpac had not voted on the proposals.

[6] Ms Gellert's affidavit also confirmed that she appeared in the High Court on Westpac's behalf on 1 August 2011 when Associate Judge Doogue heard the applications for approval of the proposals. Although Ms Gellert was noted at the commencement of the judgment to have appeared for Westpac on that occasion, Ms Gellert said that the Judge incorrectly stated in his judgment that Mrs Herbert's proposal was unopposed.

[7] An opposing affidavit was filed by Mr Nicholls, a solicitor who appeared at the hearing before Associate Judge Doogue on behalf of the trustee associated with Mrs Herbert's proposal. He produced a letter from his firm to Simpson Grierson dated 23 November 2010 enclosing Mrs Herbert's proposal and advising that the creditors' meeting was to take place at 10 am on 14 December 2010 at his firm's offices. Mr Nicholls said he signed the letter but was not personally responsible for posting it. He assumed it would have been received by Simpson Grierson in the ordinary course.

[8] He went on to say that a number of creditors opposed Mr Herbert's application in the High Court but he could not recall any party being heard in opposition to Mrs Herbert's application. He noted that Westpac had filed an appearance reserving rights in relation to Mr Herbert's application but had not filed any such document or a notice of opposition in relation to Mrs Herbert's proposal.

[9] Having decided to admit the further evidence on appeal, the next issue was whether Westpac, by its solicitors, had received notice of the creditors' meeting. We are unable to resolve that issue on the conflicting affidavit evidence. In the end, nothing turns on whether Westpac received notice of the meeting because we are satisfied on the evidence that Ms Gellert did appear at the hearing before Associate Judge Doogue on behalf of Westpac and opposed both applications. She is clear about that in her evidence which is supported by a contemporaneous newspaper report. While Mr Nicholls could not recall opposition from Westpac, his evidence does not go as far as ruling that out.

[10] The next preliminary issue was Mr Barker's submission for Mrs Herbert that Westpac had no standing to appear on the appeal. We reject that submission. In terms of s 333(2) of the Act, the Court must hear any objection made by or on behalf of a creditor before approving a proposal. On the facts as we have found them to be, Westpac did oppose both proposals. On that footing, we are satisfied that Westpac has standing to appear to oppose the appeal.

The facts in more detail

[11] Mr Herbert was a chartered accountant. The Pauanui development was driven by him and a number of his business partners. Mrs Herbert was required to guarantee some of the borrowings for the development. As the credit crisis unfolded in 2008, the development encountered significant difficulties. Despite attempts by Mr and Mrs Herbert to work with creditors to complete the development, these efforts were ultimately unsuccessful. Mr Herbert's liabilities were of the order of $29 million while those of Mrs Herbert are $10.38 million:

BNZ	$1.98m
Marac (Real Estate Credit Ltd)	$6.63m
NZ Guardian Trust	$0.9m
Westpac	$0.62m
South Canterbury Finance	$0.13m
Tarad Family Trust	$0.12m
Total	**$10.38m**

[12] Several of these creditors held mortgage securities over a property at Coatesville in which Mr and Mrs Herbert reside. Mr and Mrs Herbert are the registered proprietors of the property but hold it as trustees of a family trust associated with them and known as the Richard Herbert Family Trust. Mr Herbert is a beneficiary of that trust and Mrs Herbert may be also. BNZ held the first mortgage; the second was held by Real Estate Credit Ltd; and the third by the trustees of the Tarad Family Trust under which Mr and Mrs Herbert are beneficiaries.[2] Associate Judge Doogue appears to have accepted that the value of

[2] We were informed by counsel that the mortgage to Real Estate Credit Ltd has since been discharged but Mrs Herbert remains liable for the debt.

the property at the time of the hearing was about $2 million and that there was no equity in it. According to Mr and Mrs Herbert, their only other assets were jointly owned personal effects having a value of approximately $8,700.

[13] The proposal was that one of the trustees of the Tarad Trust, a Mr Barnes, would advance $10,000 to be available, pro rata, to all proven debts of the creditors of both Mr and Mrs Herbert. A feature of both proposals was that the insolvent would continue to make the payments required in relation to "the mortgagee" of the Albany property in which Mr and Mrs Herbert would continue to reside. There was no indication of how long this might continue. One of the creditors opposing Mr Herbert's proposal calculated that the annual interest costs on the BNZ mortgage secured over the property would be of the order of $120,000. No evidence was placed before the Court as to the source of the funds needed to make the interest payments.

[14] Section 331 of the Act provides that a creditors' proposal must be approved by 75 per cent of the creditors voting at the creditors' meeting and 50 per cent by number. Four out of six of Mrs Herbert's creditors voted in favour of her proposal, representing $9.66 million of her total debt of $10.38 million.

[15] It is not in dispute that the threshold requirements of s 331 were met. We accept that, even if Westpac did not receive notice of the meeting but would otherwise have attended and opposed the proposal, its vote would not have resulted in the threshold requirements under s 331 not being met.

The Judge's decision

[16] Mr Herbert's proposal was opposed by three creditors: Allied Nationwide Finance, the Commissioner of Inland Revenue, and Cynotech Securities Ltd. The combined debt owed to those three creditors amounted to just under $3.5m.

[17] Associate Judge Doogue's decision focused primarily on Mr Herbert's proposal. He addressed the issues under s 333(3) of the Act which provides:

333 Court must approve proposal

(3) The Court may refuse to approve the proposal if it considers that—

(a) the provisions of this subpart have not been complied with; or

(b) the terms of the proposal are not reasonable or are not calculated to benefit the general body of creditors; or

(c) for any reason it is not expedient that the proposal be approved.

[18] The first factor considered by the Judge was the size of the payment to the creditors. He accepted the estimate made by counsel for one of the opposing creditors that the dividend for creditors would be approximately 0.016 cents in the dollar. This was, the Judge considered, *de minimis* and was of no practical advantage to the creditors.

[19] The Judge did not consider that opposing creditors should be constrained to accept the amount offered. It was not conducive to the interests of the general body of creditors since it had no impact at all on their interests. There was no countervailing advantage for the general body of creditors beyond that which they might obtain upon a bankruptcy. The proposal was not reasonable within the meaning of the section.

[20] The Judge also considered that, having regard to the scale of the losses (which he considered could not be attributed solely to the unexpected onset of the global lending crisis), there was a public interest that there be scrutiny by the Official Assignee of Mr Herbert's personal conduct.

[21] Associate Judge Doogue reviewed Mr Herbert's proposal to work as a business consultant. He agreed with submissions by opposing creditors that it was undesirable for Mr Herbert to be advising others who would be involved in the sort of investment that Mr Herbert had been engaged in and which had led to his insolvency.

[22] The Judge then considered the effects of retaining the Coatesville property, expressing his views as follows:

> [24] The next point I consider is the criticism that was made about the retention of the family property at Coatesville. It may be correct that there is no equity in the property, but it also seems to be the case that such income as Mr Herbert earns will be used to service the mortgages. There is no evidence given that Mrs Herbert has any substantial source of income and the inference must be drawn that the applicant Mr Herbert alone will be funding the servicing of the mortgages. There is no reason apparent on the face of the evidence before the Court why the trustee should agree to assume the obligation of funding the applicant's housing requirements unless, of course, he expected to be reimbursed for the amounts outlaid. That is exactly the position that is going to result, I believe.
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> [25] While there can be no complaint about the secured creditors exercising their security over the property, it is difficult to see why Mr Herbert should be accepting responsibility for additional payments to the creditors who happen to have security over the family home in preference to the other unsecured creditors. That is an unsatisfactory feature of the proposal which Mr Herbert has put forward. Were Mr Herbert to be made bankrupt, such an outcome would be avoided. He would still be able to work and he could be directed to contribute to his debts.

[23] Although the Judge did not say so explicitly, it is likely he had in mind that, for the reasons he discussed, it was not expedient that the proposal be approved under s 333(3)(c). However, he might also have concluded that the retention of the Albany property was not calculated to benefit the general body of creditors because it would prefer the secured creditors over those who were unsecured.

[24] The Court then noted that although it should be slow to decline approval for a proposal accepted by the required majority at the creditors' meeting, it was still required to exercise an independent judgment. In the circumstances, the Judge found that the ground for refusing approval of a proposal under s 333(3)(b) of the Act was made out. The terms of the proposal by Mr Herbert were not reasonable and were not calculated to benefit the general body of creditors. The Judge concluded that the "palpable inadequacy" of the amount offered to the creditors was such that the Court could not approve the proposal.

[25] Associate Judge Doogue dealt briefly with Mrs Herbert's application in the following terms:

> [31] Turning to Mrs Herbert's application, I observe that that application, because it is essentially a joint proposal, cannot be treated as an independent application which could be approved even if the application by Mr Herbert were not.

> [32] But there are also the same problems of substance with that application as there are with Mr Herbert's. Given that the $10,000 is to be shared pro rata with Mr Herbert's creditors, the rate of repayment will necessarily be identical to that which Mr Herbert's creditors receive. I conclude in Mrs Herbert's case that the proposal is wholly inadequate and is not one that could be regarded as in the interests of the body of creditors as a whole nor is it reasonable. It too will be declined.

Grounds of appeal

[26] In her notice of appeal, Mrs Herbert raised two principal grounds. The first was that the Judge was wrong to conclude that the proposals were essentially jointly presented. Secondly, it was contended that the Judge was wrong to conclude that her proposal was wholly inadequate, not in the interests of the body of creditors as a whole, and not reasonable.

Discussion

[27] The principles upon which the Court approaches applications for approval under s 333 of the Act are well settled. They were recently summarised by this Court in *Magsons Hardware Ltd v Bogiatto*[3] citing particularly *Farmer v Rowley*[4] and the following passage from the judgment of Hardie-Boys J in *Re Bennetts' Proposal*:[5]

> … Rather than it being for the proponents of a scheme to show that it ought to be approved, I think the Court should accept the view of the creditors, or the majority of them, and grant approval unless it is apparent that one of the grounds for refusing approval exists. The Court is clearly required to exercise its independent judgment, for considerations of wider public interest are relevant, and therefore even unanimity amongst the creditors will not be predeterminative of approval. But unless it is clear that the creditors generally would fare better under a bankruptcy, approval ought normally to be given unless other special circumstances militate against it. Whilst a proposal ought not to be imposed upon dissentient creditors if that would be advantageous to them as members of the general body of creditors their dissent should not be upheld if to do so could be prejudicial to the general body of creditors.

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3 *Magsons Hardware Ltd t/a Mitre 10 Mega v Bogiatto* [2011] NZCA 378.
4 *Farmer v Rowley* [1992] 2 NZLR 195 (CA) at 199 – 200.
5 *Re Bennetts* HC Christchurch B138/81; M306/81, 1 February 1982 at 9.

[28] On appeal, the Court must conduct its own assessment of the evidence, giving due weight to the Judge's findings, with the appellant carrying the onus of showing the decision was wrong.[6]

[29] Dealing first with Mrs Herbert's appeal point that the Judge was wrong to conclude that her proposal could not be considered independently from that of her husband, we accept they required independent evaluation. However, there were so many points of commonality between the two proposals that considerations relevant to one were inevitably relevant to the other. The linkages between the two proposals were obvious and striking.

[30] The first common feature was that each proposal was expressed in identical terms. The same sum of money ($10,000) was offered to meet the total debts of Mr and Mrs Herbert; the outgoings on the mortgage on their jointly-owned home were to continue; and their only assets were their jointly-owned personal effects. Other common points were that the debts all arose out of the same failed joint venture and all of Mrs Herbert's debts were owed jointly with her husband. The only possible points of distinction were that Mrs Herbert's total liabilities were less than those of her husband and she may have had less involvement in the failed business venture than he did. Arguably also there was a lower risk that Mrs Herbert would engage in similar activity in future. Nevertheless, her debts at $10.38 million were still very substantial.

[31] We are satisfied the Judge was right to approach the matter in the way he did. They were effectively joint proposals with many issues common to both. But, in any event, the Judge turned his mind separately to the reasonableness of Mrs Herbert's proposal.[7]

[32] The second appeal point is that the Judge was wrong to conclude that Mrs Herbert's proposal was not reasonable and not in the interests of the body of creditors as a whole. We are not persuaded by that submission, substantially for the reasons the Judge gave.

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6 *Magsons Hardware Ltd v Bogiatto*, above n 3, at [25].

7 See the passage cited at [25] above.

[33] We agree with the Judge that the amount offered was wholly inadequate. Indeed, we would characterise it as derisory. Assuming (without evidence) that the $10,000 is available to meet Mrs Herbert's debts of $10.38 million alone, the return to creditors is about .096 cents in the dollar. This return has little or no tangible benefit to creditors.

[34] While the views of creditors will ordinarily carry substantial weight in deciding upon the reasonableness of an offer in commercial terms, the significance of this factor is undermined in this case for two reasons. First, the views of the creditors in the present case are not unanimous. Secondly, the views of the secured creditors ought to carry less weight to the extent they are secured. The secured creditors (particularly the BNZ as first mortgagee) have other means of recovering the debt due to them and are in no way reliant on the offer of $10,000 except to the extent there is a shortfall after realisation of their security.

[35] We agree that the proposal was not reasonable because it offered little material return in comparison to what creditors could expect to recover if Mrs Herbert were bankrupted. But there is a further and troubling aspect of the proposal. The proposal that the mortgagees of the Albany property (or some of them) would continue to receive interest payments of the order of $120,000 per annum represents a clear preference in favour of the secured creditors. The Court was not told how these payments were to be funded, who would be making them, or for what reason. In the absence of any evidence on these points, the Judge was right to conclude that the proposal was not in the interests of the general body of creditors.

[36] We also agree with the Judge that it is desirable in the circumstances that the Official Assignee have the opportunity to review the circumstances of the insolvency of both Mr and Mrs Herbert. As Robertson J said in *Re Nathan*:[8]

> The amount which the creditors are to receive under the proposal is infinitesimal and consequently the advantage of a pre-adjudication proposal in this case is very questionable. … The other side of the coin is that if the proposal does not go ahead the creditors may receive nothing at all. That is what Mr Nathan has said, but it may not necessarily be the case. If bankruptcy occurs the Official Assignee will be required to assess independently all claims and the background of previous dealings which

[8] *Re Nathan* HC Whangarei B53/89, 14 August 1989 at 19–20.

> may be of relevance. This could disclose a different situation. Where there is no recovery of any substance in a proposal, the possible benefits from a full and independent scrutiny are of greater significance.

[37] Given the absence of any explanation for the very unusual feature of this proposal in favour of the secured creditors, we agree that the circumstances of the case warrant review by the Official Assignee. Such an inquiry would necessarily include the source of the funds needed to pay the mortgage outgoings and the reasons for it. Is it anticipated, for example, that the secured creditors might secure additional advantages by this means that are not available to the unsecured creditors? A further obvious inquiry would be whether Mr and Mrs Herbert have other financial means available to them not yet disclosed. These considerations go to the grounds available to refuse approval under both s 333(3)(b) and (c) of the Act.

Result

[38] The appeal is dismissed.

[39] We make no order as to costs given Westpac's late decision to oppose the appeal despite its early advice it would not do so.

Solicitors:
Davies Law, Auckland for Appellant
Simpson Grierson, Auckland for Fourth Respondent