IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2014-404-64
[2014] NZHC 447

BETWEEN	SHARON LOUISE REYNOLDS ROBERT NEWCOMB LEARY and LYNETTE MAREE DUNCAN as trustees of the estate of PATRICIA AMSTEAD LEARY Judgment Creditors
AND	DOUGLAS JOHN BARTLETT (aka DOUGLAS JAMES BARTLETT) Judgment Debtor

CIV-2014-404-68

BETWEEN	SHARON LOUISE REYNOLDS ROBERT NEWCOMB LEARY and LYNETTE MAREE DUNCAN as trustees of the estate of PATRICIA AMSTEAD LEARY Judgment Creditors
AND	SHARYN DAWN BARRATT Judgment Debtor

Hearing: 10 March 2014

Appearances: G D Wiles for Judgment Creditors
A M Swan for Judgment Debtors

Judgment: 10 March 2014

ORAL JUDGMENT OF ASSOCIATE JUDGE R M BELL

Solicitors:
Duncan Horrocks Law, Epsom, Auckland, for Judgment Creditors
Whitlock & Co, Auckland, for Judgment Debtors

Counsel:
G D Wiles, Barrister, Auckland, for Judgment Creditors
A M Swan, Barrister, Auckland, for Judgment Debtors

[1] In each case the debtors have applied to set aside the creditors' bankruptcy notices. The creditors object that the applications are out of time and that there is no merit in the applications. As a second string, the debtors say that, even if they are out of time, the court should nevertheless order a stay preventing the creditors from presenting the bankruptcy applications. At this point the creditors have not filed any application for adjudication in bankruptcy.

Background

[2] The creditors obtained judgment against both debtors on a summary judgment application in CIV-2012-404-7427. Cooper J gave judgment for the creditors against the debtors on 27 August 2013 for the sum of $246,792.44 plus costs.[1] With costs, the sum owing under the judgment was $261,893.94. The creditors had sued the debtors (plus one other) for failure to settle the purchase of the creditors' property at Cliff Road, Torbay, for a price of $2,580,000. The judgment was for damages following the failure to settle and included a sum of $121,000 odd for interest, some $67,000 odd for land agents' commission and associated costs on re-sale, plus various other heads of damage.

[3] The time for appealing from the decision of Cooper J expired on 24 September 2013. The debtors did not appeal within time and they did not apply for a stay of execution. They did however instruct new lawyers. In October 2013 they applied to re-call the judgment or to correct the sealed judgment. Their aim was to obtain orders from the court that under the judgment they would not be personally liable but would be liable only in their capacities as trustees of the Barratt family trust. I dismissed that application on 8 November 2013.[2]

[4] In asking the court to rule that they were not personally liable under the judgment of Cooper J, the debtors were relying on a limitation of liability provision in clause 18 of the agreement for sale and purchase:

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[1] *Reynolds v Barratt* [2013] NZHC 2185.
[2] *Reynolds v Barratt* [2013] NZHC 2992.

18.0 Limitation of Liability

18.1 If any person enters into this agreement as trustee of a trust, then:

(1) That person warrants that:

(a) that person has power to enter into this agreement under the terms of the trust;

(b) that person has properly signed this agreement in accordance with the terms of the trust;

(c) that person has the right to be indemnified from the assets of the trust and that right has not been lost or impaired by any action of that person including entry into this agreement; and

(d) all of the persons who are trustees of the trust have approved entry into this agreement.

(2) If that person has no right to or interest in any assets of the trust except in that person's capacity as a trustee of the trust, that person's liability under this agreement will not be personal and unlimited but will be limited to the actual amount recoverable from the assets of the trust from time to time ("the limited amount"). If the right of that person to be indemnified from the trust assets has been lost, that person's liability will become personal but limited to the extent of that part of the limited amount which cannot be recovered from any other person.

[5] The debtors offered evidence that they had no right or interest in the assets of the trust and the financial records that they put forward suggested that the trust was insolvent. Their case was that, because of this provision, the creditors could not have recourse against them personally.

[6] I held that recall was not available because the judgment had already been sealed. I also held that the judgment correctly recorded the terms of the judgment of Cooper J, and there was no basis for limiting the sealed judgment in the way that the debtors contended. That was because in the summary judgment hearing, the defendants had not run a defence based on the limitation of liability provision. An application to correct a sealed judgment could not be used to alter the substantive effect of the judgment.

[7] Notwithstanding the decision on 8 November 2013, the debtors still took no steps to challenge the decision of Cooper J. Instead, there followed correspondence.

Although that correspondence is said to be on a "without prejudice" basis, it has been admitted without objection. I am satisfied that the privilege arising from "without prejudice" communications does not apply. The correspondence shows that the parties reached agreement. The agreement was that the creditors would hold their hand to allow the debtors to pay. Payment was to be made by 20 December 2013. In the event, apparently for reasons beyond the control of the debtors, they were unable to pay.

[8] In the New Year the creditors arranged for the bankruptcy notices to be issued. The bankruptcy notices were for the amounts for which judgment was entered against the debtors.

[9] Mr Bartlett was served on 20 January 2014. The time for complying with the bankruptcy notice expired on 3 February 2014. That period included Auckland Anniversary Day, but that was a "working day" under the definition in s 29 of the Interpretation Act 1999.

[10] Ms Barratt was served with the bankruptcy notice on 5 February 2014. The time for her to comply with the notice expired on 20 February 2014. That is because that period includes Waitangi Day, which is not a "working day" under the statutory definition.

[11] Mr Bartlett applied to set aside the bankruptcy notice on 3 February 2014, but his application was not served on the creditors' lawyers until 4 February 2014. Ms Barratt also applied to set aside her bankruptcy notice. That was filed in court on 20 February 2014, but the evidence from the creditors is that they did not receive her application until 26 February 2014.

[12] On 24 February the debtors filed an application with the Court of Appeal under r 29A of the Court of Appeal (Civil) Rules to extend the time to appeal against the decision of Cooper J. The grounds for appeal in their application are:

(a) There were genuine disputes of fact, despite which the court made credibility findings;

(b) The judgment was excessive in the sum of $67,548.50 (for real estate agents) which did not represent losses incurred by the respondents as a consequence of the applicant's wrongful cancellation of the agreement; and

(c) The applicants were found personally liable as trustees of the Barratt Family Trust.

[13] In the meantime, the debtors have been examined as to their assets and liabilities, and their ability to meet the judgment. There is one other judgment debtor, a Mr Harrison. He is out of the jurisdiction. Mr Swan does not have instructions for him. He has taken no steps following judgment.

[14] These questions need to be addressed:

(a) Have the debtors applied to set aside their bankruptcy notices within time? If not, what is the effect of that?

(b) (i) Is there any merit in the applications? and

(ii) Can the debtors, nevertheless, seek a halt order ahead of the creditors filing any bankruptcy applications?

Have the debtors applied within time?

[15] The relevant matter here is that the debtors' applications to set aside the bankruptcy notices were filed in court within the 10 working days for complying with the notices, but they were served on the creditors outside those 10 working days.

[16] It is well-established that the court has no discretionary power to extend the time for complying with a bankruptcy notice, nor does the court have any

discretionary power to extend the time for applying to set aside a bankruptcy notice. Section 417 of the Insolvency Act 2006 gives the court the power to extend time limits under the Act for doing any act or thing, but the case law has made it clear that time for complying with a bankruptcy notice cannot be extended.[3] There is little room for leeway in deciding whether an application to set aside a bankruptcy notice has been filed in time. It is a black-and-white decision. The matter goes to fixing the time when an act of bankruptcy has occurred. If an application to set aside a bankruptcy notice has been validly filed and served, then the time for complying with the notice is extended until the application is determined.[4] On the other hand, if there is not a valid application, then the time for complying with the notice will expire on the tenth working day after the notice was served if the notice was served within New Zealand. The act of bankruptcy will occur on the expiry of the time for complying with the notice.

[17] The question here is whether the fact that the applications were served outside the time for compliance goes to their validity. There are decisions going both ways. The decisions requiring that the setting aside application be both filed and served within the time for compliance are *Re Memelink ex parte Sanco (NZ) Ltd*[5] and *Re Guthrie ex parte Build West Ltd*.[6] A case going the other way is *Re Waruhia ex parte Next Level Finance Ltd.*[7] In that decision Judge Faire held that the High Court Rules decided whether an application to set aside has been made validly. He referred to r 237, (now r 7.19(3)) which provides that an interlocutory application is made by filing it in court. He held that service was not essential to establish when the application was made. On the other hand, in the *Memelink* case, Judge Gendall went by the form of the bankruptcy notice. The requirements for a bankruptcy notice are set by s 29 of the Insolvency Act. The form is B2 in the first schedule to

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3 *Re Dillon ex parte Blueprint Developments Ltd* HC Auckland B2164/89, 27 March 1990, Robertson J and *Alexander v S H Locke (New Zealand) Ltd* (1998) 12 PRNZ 249 (HC) (Master Gambrill).

4 High Court Rules r 24.10.

5 *Re Memelink ex parte Sanco (NZ) Ltd* HC Wellington CIV-2008-485-2691, 10 March 2009, Associate Judge Gendall.

6 *Re Guthrie ex parte Build West Ltd* HC Auckland B92/02, 23 August 2002, Master Lang (as he then was).

7 *Re Waruhia ex parte Next Level Finance ltd* HC Auckland CIV-207-404-7275, 20 February2008, Associate Judge Faire.

the High Court Rules as directed by r 24.8(3). The notices in this case followed the form in the rules. Specifically the notice under the form includes this:

> **Procedure for counterclaim**
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> If you consider you have a counterclaim, set off, cross demand against the judgment creditor that comes within paragraph 1(c), or you wish to seek the court's approval of terms of payment, you must, within 10 working days from the date of receiving this notice apply to the High Court. Your application must be supported by affidavit. You must, *within the same time*, also serve a copy of the application and supporting affidavit on the judgment creditor.
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> (Emphasis added).

Judge Gendall held that by reason of those requirements an application could not be valid if it was served outside the time laid down in the bankruptcy notice. *Re Guthrie* is to similar effect.

[18] With great respect to Judge Faire, my view is that the approach taken in the other cases is correct. I do not follow the judgment in *Re Warehuia* because it did not address the requirement in the bankruptcy notice for a setting aside application to be filed and served within the time for compliance. Again, with respect, I am not sure that his reliance on the rules for making interlocutory applications is correct, because an application to set aside a bankruptcy notice may also be heard in court as well as in chambers (as is the case in an interlocutory application). See the judgment of Heath J in *Balzat v Zhang*.[8] The better view is that a valid application to set aside a bankruptcy notice must be both filed and served within the time for compliance with the notice.

[19] The basis for requiring service on the creditor within the time for compliance is to allow the creditor to establish at the end of the time for complying with the bankruptcy notice whether an act of bankruptcy has occurred or not. The creditor then knows when time will start running under s 13 of the Insolvency Act to bring a bankruptcy application. If an application is filed and served within time, the creditor will know that the time for complying with the notice has been extended until the setting aside application has been determined.[9] Given that the purpose of

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8 *Balzat v Zhang* HC Auckland CIV-2009-404-1923, 22 September 2009.

9 High Court Rules, r 24.10.

this requirement for timely service is to bring the matter to the attention of the creditor, there may be some room for leeway in other respects. While timely service is required, it is necessary to bear in mind that frequently lawyers have to make setting aside applications within a limited time and often on very late instructions. The work often has to be carried out in something of a scramble. Under these circumstances, although an application must be served within the time for complying with the bankruptcy notice, the court may have some flexibility by applying s 418 of the Insolvency Act and following the approach taken by the Court of Appeal in *Best v Watson*.[10] Where a setting aside application is filed in court in time but there may be difficulties with service, the debtor's lawyers can make sure that they advise the creditors promptly before the expiry of time, that the application has been made, even if there is some irregularity in service. They might email or fax the setting aside application to the creditor's lawyers. It may be that at the time of service they do not know the first call date for the application and cannot inform the creditor's lawyers. Those are mere irregularities. The key thing is that they do bring the matter to the knowledge of the creditor within time. Arguments from creditors that there were irregularities in the way they were informed of the matter are not likely to be received sympathetically.

[20] I find that the present applications are not valid because they were not served within time. In the absence of any valid setting aside application, the time for compliance with the notice has not been extended under r 24.10. The debtors have already committed acts of bankruptcy.

Is there any merit in the applications? Can the debtors obtain a halt ahead of any bankruptcy applications?

[21] The debtors' applications do not rely on any of the grounds for setting aside set out in the bankruptcy notices, such as seeking the court's approval for terms of payment or that they have a counterclaim, set-off or cross-demand. Instead, they rely on the inherent jurisdiction of the court. They say that even though the setting aside applications may be invalid the court can consider in its inherent jurisdiction whether to extend relief. They invoke the court's jurisdiction to prevent an abuse of

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10 *Best v Watson* [1979] 2 NZLR 492 (CA).

process. Their case is that because the judgment against them is open to challenge - because they have arguable grounds of appeal – it would be an abuse of the process of the court for the creditors to press on with a bankruptcy application when the original judgment is still subject to appeal.

[22] On that, the creditors are relying on decisions as to inherent jurisdiction. The leading decision in this area is Master Kennedy-Grant's in *Re Wise* where he said:[11]

> Having considered the matter further, I have come to the following conclusions:
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> (a) I do have jurisdiction to grant relief to the debtors;
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> (b) The jurisdiction is the inherent jurisdiction of the court to control the abuse of process;
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> (c) The grounds on which the jurisdiction may be exercised are:
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> (i) Procedural defect in the obtaining of the judgment on which the bankruptcy notice is based; and/or
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> (ii) The existence of arguable grounds of defence to the claim for which judgment is given.
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> (d) The grounds on which the judgment may be exercised may extend beyond those stated in (c) to any ground on which the court feels it necessary to intervene to prevent injustice but I make no finding on that point in this judgment.
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> (e) The correct procedure for invoking the inherent jurisdiction of the court is not the filing of an affidavit under r 41 but the filing of an interlocutory application to set aside the bankruptcy notice on one of the grounds stated in (c) and/or possibly the broader grounds stated in (d) above.

[23] It is necessary to put that statement into context. He was dealing with a typical situation where creditors had obtained a judgment by default and the debtors then sought the opportunity to apply to the court in which judgment was given against them, to have that judgment set aside. With great learning, Master Kennedy-Grant established a basis for invoking the court's inherent jurisdiction to grant the debtors that opportunity. He held that the grounds for invoking the jurisdiction might arise if there had been a procedural defect in obtaining judgment or if there were arguable grounds of defence to the claim for which judgment was given.

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[11] *Re Wise* HC Auckland B227-228/95, 21 June 1995 at 6.

[24] That was in the context of default judgments. As is well established in cases such as *Russell v Cox*[12] the court may set aside a default judgment if it is necessary to avoid a miscarriage of justice. A miscarriage of justice may occur if there are arguable grounds of defence even if judgment was regularly obtained.

[25] This however is not a case of a default judgment. The debtors referred to *Krukziener v Hanover Finance Ltd*.[13] That case appears to be an extension of the approach taken by Master Kennedy-Grant in *Re Wise*, in that Mr Krukziener was applying to set aside a judgment given against him even though he had opposed the original summary judgment application. I note that in the event Mr Krukziener was not successful. But, with great respect, that judgment seems to have overlooked the difference between a judgment by default and a judgment which has been given after the debtor has used the opportunity to contest the case against him.

[26] I put the matter this way. In bankruptcy law, courts may at times look behind a judgment. But courts are more ready to look behind a judgment when it is a default judgment than one which has gone to trial and there has been a full hearing on the merits. In this regard I refer to a decision of the High Court of Australia, *Corney v Brien*.[14] Fullagar J indicated that a court would look behind a judgment after a trial on the merits only if there was a prima facie case of fraud or collusion or miscarriage of justice. It is difficult to say that in this case any of those matters are satisfied here. The most that can be said for the debtors is that their lawyers failed to raise arguments that might have been available to them.

[27] It may be that the inherent jurisdiction of the court is not as narrow as laid down by Master Kennedy-Grant in *Re Wise*. But it is necessary to bear in mind that the exercise of that power is to prevent an abuse of process. I look at this case with that in mind. The creditors have obtained a judgment. They have also established an act of bankruptcy. Time is now running against them to file any bankruptcy applications. Under s 13 they have only three months in which to apply. If I were to make any order now, staying them from taking any steps by way of a bankruptcy application, I would be deciding now, and finally, that they should not apply for the

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12 *Russell v Cox* [1983] NZLR 654 (CA).
13 *Krukziener v Hanover Finance Ltd* HC Auckland CIV-2007-404-2896, 12 August 2008.
14 *Corney v Brien* [1951] HCA 31; (1951) 84 CLR 343 at 356-8.

debtors' adjudication in bankruptcy – at least not without establishing a fresh act of bankruptcy.

[28] The debtors referred to cases where courts have made such stay orders ahead of any application for bankruptcy being filed. The two cases are: *Holloway v Darby*[15] and *Re Taylor*.[16] In both those decisions on setting aside applications, the Judges were satisfied that the creditors should not be allowed to present bankruptcy applications and they ruled accordingly, ahead of any such applications being filed. I am not satisfied that this is an appropriate case in which I should make any such order.

[29] The debtors have applied for an extension of time to appeal the decision of Cooper J. The debtors are well out of time. There are a number of matters that the debtors will have to overcome to persuade the Court of Appeal that they should have an extension of time. First, there is the lapse of time and the steps that have been taken in the meantime. The debtors may persuade the Court of Appeal that they were in genuine doubt as to their personal liability under the judgment of Cooper J. But they could not have been under any mistake after 8 November 2013. They then entered into settlement arrangements to pay off their liability under the judgment. It was only after their attempts to settle proved abortive that they turned their minds to appeal. There are decisions of the Court of Appeal on applications to extend time where the Court has considered that the fact that a decision to appeal has been made only as a result of subsequent events has counted against an application to extend time. I have in mind cases such as *Thompson v Turbott*, *Email v Fisher & Paykel Ltd* and *Donaldson v Green Juice Co Ltd (In Rec).* [17]

[30] Second, the debtors will have to persuade the Court of Appeal not only that they can introduce a new ground of defence but that, to allow that new ground of defence to be considered, they will also have to rely on fresh evidence. They will face the enormous difficulties of trying to persuade an appellate court to accept evidence that was not considered at first instance.

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15 *Holloway v Darby* HC Hamilton CIV-2005-419-1085, 8 December 2005, Associate Judge Faire.
16 *Re Taylor* (1992) 4 NZBLC 102,875 (HC).
17 See *Thompson v Turbott* [1963] NZLR 71 (CA), *Email v Fisher & Paykel Ltd* [1991] 1 NZLR 569 (CA) and *Donaldson v Green Juice Co Ltd (In Rec)* (1995) 8 PRNZ 409 (CA).

[31] Third, they will have to persuade the Court of Appeal that there is merit in their appeal.

[32] It is uncertain whether the debtors will succeed in their application to obtain an extension of time in the Court of Appeal. It is not for me to predict which way the Court of Appeal will decide the application. Because it remains a possibility – and a real possibility – that the application may not succeed, there is a risk of real prejudice to the creditors if they were to be prevented from beginning bankruptcy proceedings now while the question of extension of time remains at large before the Court of Appeal. Mr Swan advised that the application to extend time is not likely to be heard in the Court of Appeal until June of this year. By then the time for the creditors to file their bankruptcy applications will have expired. In my view, the better course is to dismiss the setting aside/halt applications now and allow the creditors to file their bankruptcy applications. Any requests for time to await a decision of the Court of Appeal can be considered as part of the case management of the bankruptcy applications. Specifically, once an application is on foot, the court has powers under ss 38 and 42 of the Insolvency Act to determine whether the applications should be put on hold to await the outcome of the Court of Appeal's decision on the application under r 29A of the Court of Appeal (Civil) Rules. I indicate, for everyone's assistance, that it may be convenient for any bankruptcy applications to come before me given my present familiarity with these issues.

Outcome

[33] For these reasons, I dismiss the debtors' applications to set aside, but in dismissing them I record that that is without prejudice to the rights of the debtors to apply later - when there are creditors' applications on foot - for a halt under ss 38 and 42 of the Insolvency Act.

[34] Mr Wiles seeks costs. I order costs on a 2B basis. I am sure that counsel will be able to calculate costs themselves, but if there is any difficulty they may file memoranda.

[35] I also record that this case has been heard in court.

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Associate Judge R M Bell