IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2015-404-864
[2016] NZHC 2738

BETWEEN	KIWI BEST REALTY LIMITED (IN LIQUIDATION) Plaintiff
	VIVIEN JUDITH MADSEN-RIES AND HENRY DAVID LEVIN as Liquidators of Kiwi Best Realty Limited (In Liquidation) Second Plaintiffs
AND	JUMSHIED HUSSAIN KASHKARI Defendant

Hearing: 25 - 28 October 2016

Appearances: P V Shackleton and E E Meade for the Plaintiffs
ASR Kashyap for the Defendant

Judgment: 15 November 2016

INTERIM JUDGMENT OF MUIR J

This judgment was delivered by me on Tuesday 15 November 2016 at 3.30 pm
Pursuant to Rule 11.5 of the High court Rules.

Registrar/Deputy Registrar

Date:…………………………

Counsel/Solicitors:
P V Shackleton, Meredith Connell, Auckland
E E Meade, Meredith Connell, Auckland
ASR Kashyap, Barrister, Auckland

Introduction

[1] The plaintiffs, Kiwi Best Realty Limited (In Liquidation) (the Company), and its liquidators Ms Madsen-Ries and Mr Levin seek orders pursuant to s 301(1)(b) of the Companies Act 1993 (the Act) that the Company's director, Mr Kashkari, pay compensation for breach of duties owed under ss 131(duty to act in good faith), 135 (not to trade recklessly) and 136 (duty not to incur obligations without belief in reasonable grounds of performance).

History of the company

[2] The Company was incorporated on 10 August 2007 with the intention of operating as a real estate business. It entered into a five year franchise agreement with the REMAX Property Group and took premises in Henderson, the lease of which was guaranteed by Mr Kashkari.

[3] It did not commence trading until approximately one year later because of uncertainties created by the GFC, which had, in the interim, impacted the economy. Mr Kashkari was, from the company's inception, both a director and shareholder. Originally, he was joined by Mr Rajneel Raj but Mr Raj resigned as a director on 30 January 2008 and, according to Companies Office records, "vacated" his shareholding on 23 November 2011.

[4] On 26 September 2014 the company was liquidated on the petition of the Commissioner of Inland Revenue (IRD). At that time it is common ground that creditors totalled $664,504.74. Of this, the amount of $620,210.99 was owed to the IRD for arrears of GST, PAYE, student loan deductions and income tax, together with associated penalties and interest. The balance of the company's debts at the date of liquidation were current.

[5] The debts to the IRD comprised:

(a) Goods and services tax owing for various periods between 31 March 2009 and 31 January 2013 comprising a core debt of $66,005.96 and interest and penalties of $59,082.52 (total $125,088.48).

(b) PAYE tax owing for various periods between 31 March 2009 and 31 December 2013 comprising core tax of $141,724.42 and interest and penalties of $336,313.57 (total $478,037.99)

(c) Student loan employer deductions owing for various periods between 30 April 2010 and 31 January 2014 comprising core debt of $4,411.57 and interest and penalties of $8,191.71 (total $12,603.28)

(d) Income tax owing for the period 31 March 2010 to 31 March 2013 (total $137,063.00)

[6] No financial statements were prepared by the company until 2014. When completed, these indicated the following trading positions:

	FYE 2009 $	**FYE 2010 $**	**FYE 2011 $**	**FYE 2012 $**	**FYE 2013 $**	**FYE 2014 $**
Gross revenue	197,436	433,091	259,629	482,152	548,428	520,014
Net surplus (deficit)	427	24,080	(50,003)	14,806	(3,265)	(84,122)

[7] Over the same period, the accounts reported the following working capital and net assets/liabilities:

	FYE 2009 $	FYE 2010 $	FYE 2011 $	FYE 2012 $	FYE 2013 $	FYE 2014 $
Total Current assets	101,441	58,238	9,359	80,413	51,489	93,959
Total Current liabilities	90,456	15,940	11,960	66,197	24,934	148,343
Working Capital	10,985	42,298	(2,601)	14,216	26,555	(54,384)
Non-Current Assets	85,334	69,133	58,024	54,521	66,391	61,184
Non-Current Liabilities	20,481	11,513	5,508	4,016	2,025	0
Net Assets/Liabilities	75,839	99,919	49,916	64,721	90,921	6,799

[8] As at the date of liquidation, the company had minimal physical assets. A shelf and chairs were sold for $730 and a 2004 Mitsubishi car for $3,000. In addition the liquidators recovered commissions owing to the company of $19,768.50.

[9] The company's only other realisable asset was the current account owed by Mr Kashkari. This had fluctuated over time. For the year ending 31 March 2009 it was in credit for $83,321.00. Thereafter, Mr Kashkari became a debtor of the company, with current account liabilities climbing from $10,523.00 for the year ending 31 March 2010 to $184,342.00 for the year ending 31 March 2013. In the following year that debt was reduced to $94,579.00. For the period between 1 April 2014 and the date of liquidation further debts accrued, with the result that by 24 September 2014 Mr Kashkari's current account stood at $111,728.00.

[10] Within approximately two hours of the appointment of liquidators, Mr Kashkari paid the sum of $120,000.00 to IRD believing his current account was in approximately that amount. This payment was in turn transferred to the liquidators' trust account on 23 October 2014. No current account claim is therefore made by the liquidators. Indeed, the plaintiffs accept that a credit of $8,272.00 is appropriately given against any sum for which Mr Kashkari is found liable.

[11] Repayment of the current account was facilitated by Mr Kashkari borrowing from a family trust which was in turn able to refinance a property as a result of the rising Auckland market. In evidence Mr Kashkari was candid that it was not until approximately the end of the 2014 financial year that he was in a position to repay the current account. I accept therefore that, in terms of the company's working capital requirements and ability to meet its obligations as they fell due, the so called "current account" could not properly be considered a current asset prior to that point in time. On that basis, the company had significant deficits in working capital from year end 2011 onwards, reaching $157,788.00 in year end 2013. It was also balance sheet insolvent from year end 2012, even without bringing to account the significant penalties and interest which had accrued on the IRD debt by that time.

[12] The total amounts recovered in the liquidation (approximating $140,000.00) have, according to evidence from Mr Levin, been wholly expended in liquidators' and solicitors' costs, with the result that IRD has received no payment against its debt (for a significant part of which it stands as a preferential creditor).

[13] The trading history of the company shows that from a very early stage in its history it was, in terms of the solvency test in s 4 of the Act, unable to pay its debts as they became due in the normal course of business.[1] IRD's "case tracking action detail" dated 10 July 2009 indicates by that stage the company had arrears of GST of $6,943.07. The relevant note records that the company had no funds to pay off any part of the debt immediately and wished to enter into an instalment arrangement. That arrangement was confirmed by IRD correspondence dated the same date and was in terms that the debt would be paid by 15 monthly instalments of $500.00 and a final instalment of $253.17.

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[1] In his evidence Mr Levin says that the company was insolvent, in the sense of unable to pay its debts as they fell due from "at least 31 March 2009". I consider him likely to be correct in that regard. The date of insolvency is not, however, the date from which assessment of losses for the purposes of s 301 should necessarily take place (see *Madsen Ries v Petera* [2015] NZHC 538 at [97]).

[14] That arrangement was not adhered to. The action detail for 22 September 2009 records that the debt had, by that stage, increased to $10,654.37. It also records the company would catch up with the missed instalments and additional arrears within the next four weeks.

[15] Soon after, the company fell into default in filing GST returns. It was first notified of such default on 17 November 2009. By October 2012 there was some 16 GST returns (each required to be filed on a two monthly basis) outstanding. By the same date, 10 PAYE returns and six income tax returns had not been filed. All the while interest and penalties continued to accrue.

[16] By the beginning of 2013 the debt exceeded $200,000.00 and by 2014 $500,000.00. Although from approximately March 2013 the company did begin to lodge regular GST and PAYE returns and pay what was required of it, the historic debt simply compounded with accruing penalties and interest. A letter prepared by the company in May 2014 records that, of all the core tax liabilities incurred by it between March 2009 and January 2014 (totalling $230,971.03), only $17,232.89 had been paid. By the same date, the letter acknowledges penalty and interest liabilities totalled an additional $366,559.75.

[17] Ultimately this burden of IRD debt proved insurmountable. Although efforts were made to settle on terms that the company pay $180,000 immediately and a further $72,000 by 36 monthly instalments of $2,000 these were rejected by IRD and liquidation on its petition followed almost immediately.

The claims under sections 131, 135 and 136 of the Act

[18] It is convenient to deal with these claims together because, as in *Madsen-Ries v Petera*[2] the allegations underpinning each claim are essentially the same.

[19] The liquidators rely on the company's insolvency from early 2009 and the fact that it continued to trade despite the fact that month on month it was unable to meets its tax obligations and only survived by application of monies (GST and

[2] *Madsen-Ries v Petera* above n 1.

PAYE) held on trust for IRD to its other more pressing trade creditors. They say that its problems were compounded by the fact that Mr Kashkari withdrew money from the company for his day to day living expenses when such funds should have been applied to its tax liabilities. They make that submission despite the fact that the current account was ultimately repaid, relying particularly on the fact that from year ended 2010 to year ended 2013 inclusive, the current account debt increased significantly, during which period no tax was paid or returns filed.

[20] The liquidators also point to the absence of returns over an extended period and the fact that, on liquidation, various correspondences from IRD remained unopened as indicating a "head in sand" approach totally inconsistent with Mr Kashkari's duties. They say that nowhere is there evidence of the "sober assessment" the authorities require,[3] or even preparation of the cash flow or management reports on which such an assessment could be based. They point out that not until 2015 were accounts for the relevant periods actually prepared. Although they do not challenge Mr Kashkari's veracity when he says he did ultimately hope to make his peace with IRD through some form of settlement, they say that for five years or more he allowed hope to triumph over reality. Finally, they emphasise that Mr Kashkari's exposure to personal guarantees under the company's lease arrangements placed him in a conflicted situation which may at least in part explain why he continued to trade a clearly insolvent company.

[21] By contrast, Mr Kashkari argues that the company's interests were best served by prioritising trade creditors for sufficient time to allow the real estate market to improve and then attempting to negotiate a deal with IRD. He highlights the fact that in 2009 he had booked 20 sales in a proposed development which, on account of the GFC, did not ultimately proceed and that, in the same year, 14 conditional sales "fell over" because of the economic uncertainties. He says that while his basic family requirements were indeed met by the business, these were modest, that the wages he took from the business were less than $30,000.00 over the whole five year period and that in respect of sales where he was either the listing or selling agent, he chose to leave his commission entitlements in the company. He emphasises the company's compliance with its obligation from 2013 onwards and

[3] *Sojourner v Robb* [2008] 1 NZLR 751 (CA) at 25.

his desire thereafter to try to reach an accommodation with IRD, albeit that this would have necessitated very substantial discounts on what was then owing. Finally, he points to a change of agency from REMAX to Ray White at the point his REMAX agency expired, the more favourable terms he was able to negotiate as a result and the company's move from Henderson to New Lynn as examples of his commitment to exploring all possible means of rehabilitating the company's fortunes.

Sections 131, 135 and 136 – the tests

[22] Section 131(1) imposes a duty on a director of a company when exercising powers or performing duties to act in good faith in what the director believes to be the best interests of the company. As observed in *Sojourner v Robb* the test comprises an amalgam of objective and subjective elements:[4]

> [102] … the standard in s 131 is an amalgam of objective standards as to how people of business might be expected to act, coupled with a subjective criteria as to whether the directors have done what they honestly believe to be right. The standard does not allow a director to discharge the duty by acting with a belief that what he is doing [is] in the best interest of the company, if that belief rests on a wholly inappropriate appreciation as to the interests of the company….

A breach of s 131 involves a breach of fiduciary obligation.[5]

[23] Section 135 of the Act prohibits a director from engaging in reckless trading. The duty contained in s 135 reflects a director's fundamental duty to protect the interests of creditors when the company approaches insolvency.[6]

[24] In *Mason v Lewis* the Court of Appeal noted the "essential pillars" of s 135 as:[7]

> (i) the duty which is imposed by the section is one owed by directors to the company (rather than any particular creditors);
>
> (ii) the test is an objective one;

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4 *Sojourner v Robb,* above n 3 at [102].
5 *Morgenstern v Jeffreys* [2014] NZCA 449 at [99].
6 *Sojourner v Robb,* above n 3 at [25].
7 *Mason v Lewis* [2006] 3 NZLR 255 (CA) at [51].

> (iii) it focuses not on the director's belief but rather on the manner in which the company's business is carried on, and whether that modus operandi creates a substantial risk of serious loss; and
>
> (iv) what is required when the company enters troubled financial waters is …
>
> > (a) "sober assessment" by the directors, we would add of an ongoing character, as to the company's likely future income and prospects.

[25] Section 136 prohibits a director from agreeing to the company incurring an obligation unless the director believes at the time on reasonable grounds the company will be able to perform the obligation when it is required to do so. Again, the test contains an amalgam of subjective and objective elements. The question is whether the director agreed to the company incurring an obligation at a time when he or she did not believe (a subjective test) on reasonable grounds (an objective test) that the company would be able to perform that obligation when required to do so.[8]

Analysis – liability

[26] I accept the liquidators' submission that Mr Kashkari was in breach of one or more of ss 131, 135 or 136 from an early stage in the company's trading history. As in *Madsen-Ries v Petera*, I find his decision to pay trade debts and not to pay outstanding GST and PAYE liabilities, or even to file returns for an extended period, a "serious error of judgment"[9] on his part. His decision to do so resulted in a rapidly escalating debt by virtue of the imposition of penalties and interest. He was aware that this was the case but chose to live in hope that, if only he could trade the company through the worst of the GFC, he could at some stage enter into compromise with IRD which had it accepting a very significant discount on the accrued position.

[27] Although I accept that Mr Kashkari fully intended that his company meet at least the core IRD debt as and when it could, if necessary by the introduction of additional capital or repayment of his current account when he was personally in a position to do so, his was indeed a triumph of hope over reality. By failing to pay one of the company's most important creditors and applying money the company

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8 *Fatupaito v Bates* [2001] 3 NZLR 386 (HC) at 80.

9 *Madsen-Ries v Petera* above n 1, at [68].

held on trust for IRD to meet the calls of other creditors and his family's living costs, he cannot be held to have acted in good faith in what he believed to be the best interests of the company, bearing in mind the element of objectivity implicit in the test. It was demonstrably not in the interests of the company to allow its liabilities to escalate rapidly through non-payment of IRD, still less to compound its problems through non filing of returns. To the extent Mr Kashkari may have had an honest belief to the contrary, I find that rested on an inappropriate appreciation of the company's interests.

[28] In short, the course he chartered meant that the company was always going to be dependent on the largesse of probably its most important creditor when any good will the company had with that creditor had been significantly eroded by persistent non-adherence to instalment payment arrangements and a serial failure to file returns and accounts. No reasonable director could have considered that appropriate. Mr Kashkari's own acknowledgment in his undated correspondence to IRD shortly before liquidation that he had "failed in the past" is in my view a fair assessment. When the company became insolvent Mr Kashkari's obligation was to stop making drawings on his current account, to realise the assets of the company (including recovering debts owed by him) and to prepare realistic forward projections on which to base a "sober assessment" of the company's future. He did none of this. I accordingly find that he acted in breach of his obligations under s 131.

[29] For similar reason I also find him in breach of s 135. In continuing to trade the business as he did he created a substantial risk that the IRD would suffer serious loss. As in *Madsen-Ries v Petera*,[10] he was well aware of that risk but elected to run it for a significant period – the risk ultimately becoming reality with liquidation of the company. Again, he never undertook the objective assessment required, preferring instead to live in hope that things would turn around and a compromise struck.

[30] I consider him also in breach of s 136. He was aware that for every month the business traded it incurred both fresh GST and PAYE liabilities and penalties and interest on accrued debts. His decision as director to continue in business can in my

10 *Madsen-Ries v Petera* above n 1.

view be considered an agreement that the company incur all such liabilities. Nor could he have believed on reasonable grounds that the company was able to meet these obligations when, month on month, it conspicuously did not have the liquidity to do so. The decision to suspend filing returns is one only explicable in the context of a director fully aware that, if the ongoing liabilities were not compromised, there would be no ability to meet them. And again, the absence of any evidence that Mr Kashkari realistically considered the company's trading and cash flow position and prospects is telling. Instead he simply chose to "hunker down" in the hope all would somehow work out in the end.

[31] In considering each of these breaches I assess the operative date as 31 December 2009. In doing so I am conscious of the fact that the company was probably insolvent in a s 4 sense upwards of six months earlier. However, as Lang J noted in *Madsen-Ries v Petera*:[11]

> [97] … The courts have recognised that directors are not required to ensure that a company ceases to trade the moment it becomes insolvent [Citing *Richard Geewiz Consultants Ltd (In liquidation) v Gee* [2014] NZHC 1483 at [99]]. There are limits, however, to the extent to which the directors can permit a company to continue trading in the hope that things will improve. The justification for such hope is also likely to be less where the company is indebted to the Commissioner for unpaid PAYE or GST, because such payments are only meant to be held for a short time before being paid to the Commissioner [Citing *Richard Geewiz Consultants Ltd (In liquidation) v Gee* at [100].

[32] By July 2009 the company was already indebted for PAYE and GST deductions of $7,753.17. An instalment arrangement reached that month, despite requiring only a modest monthly payment of $500, was almost immediately the subject of default. At this point Mr Kashkari needed to take urgent steps to both assess whether the company could realistically meet its existing and accruing debt and to prepare realistic forecasts relating to future profitability and cash flow. He then needed to monitor strictly adherence to these forecasts to determine their realism or optimism. I consider an allowance of four months for that purpose generous but adopt 31 December 2009 as the operative date in that, by that time, Mr Kashkari was also in a position realistically to assess the implications of the failed residential development the company had been representing and of the various

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11 *Madsen-Ries v Petera* above n 1.

conditional sales which had fallen over. In so doing I give Mr Kashkari the benefit of what I consider to be all reasonable allowances.

The quantum of compensation

[33] Section 301(1)(b)(ii) provides that where negligence, default or breach of duty or trust has been established on the part of a director the court may order that person:[12]

> to contribute such sum to the assets of the company by way of compensation as the court thinks just.

[34] The approach to the assessment of compensation is now well established. It starts by establishing a date from which inadequate corporate governance has become evident. I have already assessed that date as being 31 December 2009. It then focuses on three factors – causation, culpability and the duration of trading as relevant to the exercise of the Court's discretion.[13] Finally, it recognises that claims of this character necessarily have to be dealt with in a relatively broad brush way, given that the jurisdiction to order recompense is of an "equitable" character.[14]

[35] In *Löwer v Traveller* the Court of Appeal identified the element of causation as concerned with the link between the carrying on of the business recklessly (to the knowledge of the impugned director) and the indebtedness of the company for which it is sought to impose personal liability.[15]

[36] As to culpability, it identified that this was linked to the deterrent purpose of the provision. It said that this factor called for an assessment of the blameworthiness of the director's conduct bearing in mind a continuum between blind-faith or muddle-headedness at one end and plainly dishonest conduct at the other. It noted that the deterrent purpose of the section is served in cases involving a high degree of culpability by orders which are punitive as well as compensatory.[16]

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12 Companies Act 1993, s 301(1)(b)(ii).
13 *Mason v Lewis*, above n7, at [109] – [110].
14 *Mason v Lewis,* above n 7, at [118].
15 *Löwer v Traveller* [2005] 3 NZLR 479 at [70].
16 *Löwer v Traveller,* above n 15, at [83].

[37] In respect of the duration of the wrongful conduct, the Court in that case noted a period of breach of two years and 10 months as being "lengthy".

[38] In the present case I agree with the liquidators that Mr Kashkari's decision to continue trading from the date I have established he was in breach of his duties, together with his decision to take money from the company for personal and family expenses when its first obligation was to meet the trust imposed on its PAYE deductions and GST collections, provides the necessary causal link to the losses accruing from that date.[17]

[39] I am also satisfied that although Mr Kashkari was not dishonest (other than in the equitable sense that he knowingly allowed the company to breach the trust imposed on the deductions and collections) and although he does appear to have made reasonably modest calls on the company and not withdrawn personal commission entitlements, nevertheless his level of culpability is moderate. His directorship of the company went beyond muddle-headedness. He made a deliberate decision to use monies held on trust for IRD to finance his more pressing trade creditors and his household. At the point the company clearly had no capacity to meet its ongoing liabilities he suspended filing returns. He never prepared the cash flow forecasts essential if he was to make any sober assessment of the company's fortunes. Instead, he buried his head in the proverbial sand entertaining the honest but ultimately hopeless belief that he could, in due course, come to some accommodation with the Commissioner. The deterrent provisions of the jurisdiction are relevant in that context.

[40] Finally, as to duration, it is clear that the company was insolvent for much of its six year trading history. I have found that for over four years of that Mr Kashkari was in breach of his duties. Although the company did adopt a more compliant profile in the last 18 months of its existence, the damage had already been done to the extent accrued liabilities, including penalties and interest, meant that its position was hopeless. On any analysis the duration of default was lengthy.

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[17] That conclusion is reached irrespective of the different causation tests applicable to breaches of s 131 (on the one hand) and ss 135 and 135 (on the other) as discussed by the Court of Appeal in *FXHT Fund Managers Ltd (in liq) v Oberholster* [2010] NZCA 197 at [28].

[41] Cumulatively, these factors favour a significant award of compensation for the additional losses the company sustained by trading beyond 31 December 2009 (as compared with a notional liquidation at that date). The liquidators did not advance a notional liquidation model. They sought an award equivalent to the total value of creditors outstanding. This included IRD debts predating 31 December 2009, on the basis that the company was insolvent from, at the latest, 31 March in that year. Although the core debt, penalty and interest owing to IRD will need to be recalculated based on the later start date I have identified, I accept such sum as a reasonably proxy for the loss suffered by the company as a result of the decision to continue to trade in breach of duty. I do not include the other trade debts at the date of liquidation as it was always Mr Kashkari's reasonable expectation that they be met and broad equivalents can be assumed in a hypothetical 31 December 2009 liquidation.

[42] Against that background, the authorities require me to stand back adopting a broad, global approach mindful of the overall equities.

[43] In that respect Mr Kashyap relies heavily on the observations of Miller J in *Kings Wharf Coldstore Ltd (in Receivership & Liquidation) v Wilson* in terms:[18]

> … the essential task is to compensate whatever real loss or detriment the company may have suffered, subject to equitable discretionary consideration of "conscience, fairness and hardship and other features such as laches and acquiescence": [Citing *Chirnside v Fay* [2004] 3 NZLR 637 at [66], [67], citing Somers J in *Day v Mead* [1987] 2 NZLR 443 at 462]. This approach is consistent with s 301, which allows the Court to order such compensation as it thinks just.

[44] Mr Kashyup's principal argument (albeit one which he fairly recognised undermined his defence of the breach of duty arguments) is that the company's defaults in its obligations to the IRD were so egregious and longstanding that the IRD should have much sooner liquidated the company, with the result that liability for the compound interest and penalties now faced by Mr Kashkari would be

18 *Kings Wharf Coldstore Ltd (in Receivership & Liquidation) v Wilson* (2005) 2 NZCCLR 1042 at [113]. In Watts, Campbell, Hare *Company Law in New Zealand* (2nd ed, LexisNexis NZ Limited, Wellington, 2016) at [13.6] Peter Watts QC argues that equitable discretionary considerations are not appropriately considered in this context because, inter alia, not all directors' duties are fiduciary in nature – the insolvency duties under ss 135 and 136, in particular, having no direct common law or equitable parallel.

significantly less. He says that by indulging the company for so long IRD gave oxygen to Mr Kashkari's belief that a deal might be done and that therefore in equity an adjustment should be made to the compensation payable.

[45] I have some sympathies for this argument at a factual level. Although on 10 October 2012 IRD had written to the company in what it styled a FINAL NOTICE, identifying the six income tax, 16 GST and 10 PAYE returns which were outstanding and the fact that criminal charges could follow, it was not until almost two years later that it brought liquidation proceedings.

[46] Mr Shackleton emphasises Mr Kashkari's concession under cross-examination that IRD could not be aware of the full tax position until returns were filed,[19] that this did not occur for any of the years in question until May 2014 and that, even then, IRD still required further documents, including bank statements that were not provided until August. I accept that submission but still regard as inexplicable why, in the face of serial failure to provide returns, IRD had not, at least two years earlier, made default assessments and wound the company up.

[47] However, because the duties owed under ss 131, 135 and 136 are owed to the company rather than any particular creditor there are conceptual difficulties with how the imprudent conduct of a particular creditor mitigates a defendant's liability. Anderson J addressed that issue in *Nippon Express New Zealand Ltd v Woodward* in terms:[20]

> At the heart of a director's liability pursuant to s 275(1)(b)(ii) is the concept of compensation to the company for a director's breach of duty to the company. The damage to the object of the duty, namely the company, is the debt which the company has been plunged into. Although such damage to the company has led to loss by the plaintiff [a creditor] no duty was owed by it to the company itself. It is not the plaintiff but the directors whom the law expects to be the company's keeper.

[48] These observations were adopted by O'Regan J in *Fatupaito v Bates*[21] and in *Lewis v Mason*[22] the Court of Appeal expressed doubt whether issues of contributory

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19 NOE 95/22.
20 *Nippon Express New Zealand Ltd v Woodward* (1998) 8 NZCLC 261,765 at 261,778.
21 *Fatupaito v Bates* above n 8, at [93].
22 *Lewis v Mason* [2009] NZCA 306 at [109].

negligence were relevant to an order for compensation made under s 301, particularly where there were multiple creditors the innocent among whom would be effectively penalised by the default of one.

[49] Nevertheless, there have been cases where awards have been reduced on account of creditor action or inaction. In *Re Cellar House Ltd; Walker v Allen*,[23] for example, Ellen France J made a substantial allowance to take account of the fact that the most significant debt ($8,581,024.00) was owed to the Customs Department for excise duty which had, with penalties, ballooned from an initial liability of approximately $1,400,000.00 only.[24] Her Honour held that:

> ... While Customs' delay is not a factor which could give rise to an affirmative defence, it must be relevant in considering the amount now appropriately payable by Mr Allen.

[50] This decision was not specifically disapproved of in *Lewis v Mason*. Indeed, the Court indicated that, despite its earlier observations:[25]

> We can see that that is a stronger case for taking into account the contributory conduct by a creditor where that creditor will be the only beneficiary of an award and any reduction in the amount which would otherwise be awarded has no effect on other creditors.

[51] In the present case (more so even than in *Walker v Allen*) one creditor (IRD) dominates the liquidation[26] and the consequences for other creditors of any reasonable reduction in an award of compensation on account of IRD delay is modest, particularly having regard to its (in part) preferential status.

[52] Ultimately what I am required to do is to establish a measure of compensation which is just based on a global assessment of all relevant factors. Mr Kashkari's conduct, although clearly unsatisfactory, was certainly not at or near the highest levels of culpability. Making allowance for timely repayment of his current account, he derived only minimal personal benefits from the company and he took

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23 *Re Cellar House; Walker v Allan* HC Nelson CP13/00, 18 March 2004. See also *Re Petros Developments Ltd* HC Auckland CRI-2003-404-633, 15 December 2004, Keane J.

24 Other debts comprised IRD ($2,706,738.00) and trade creditors ($176,302.00).

25 *Lewis v Mason*, above n 22, at [109].

26 It comprises 93.3% of all creditors. By contrast, the Customs Department debt in *Re Cellar House; Walker v Allen* , above n 23, was 77.4% of total debt.

several important steps designed to improve the performance of the business. Nor did he withdraw his personal commission entitlements.

[53] Moreover, I am in no doubt that he had an honest intention that the company meet at least its core liabilities as soon as its performance permitted or his personal or family position improved sufficiently for further capital introductions to be made. An open offer was ultimately made with that broad intention and effect.

[54] I am, to a lesser extent, also influenced by the wide disparity between the core debt owed to IRD and the total debt, including compound penalties and interest, in circumstances where I find it inexplicable the company was not wound up sooner.

[55] I am conscious of the fact that the mathematics of deriving the ultimate compensation figure cannot in Ellen France J's words be "very scientific",[27] and indeed that, as William Young J put it in *South Pacific Shipping Ltd v Trevellen and Waller*, "some element of rough justice may be called for". [28]

[56] In my view a just result sees deducted from all debts incurred to IRD from 1 January 2010 an amount of 25 per cent to reflect these considerations. New calculations will be required by the liquidators for this purpose. The present judgment is issued on an interim basis pending such calculations.

Result

[57] I give judgment in favour of the plaintiffs for a sum representing total debt incurred by the company to IRD from 31 December 2009 (together with interest and penalties thereon as calculated by IRD from time to time) less:

(a) 25 per cent of that amount; and

(b) the sum of $8,272.00 being Mr Kashkari's overpayment in respect of his current account.

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27 HC Christchurch, CIV-1998-409-000069, 12 February 2004 at [163], albeit in the context of s 305.

28 *South Pacific Shipping Ltd v Trevellen and Waller* HC Christchurch CIV-1998-409-69, 12 February 2004.

[58] The liquidator is, within 21 days, to provide an affidavit with the necessary calculations. The defendant may respond within seven days. I will then issue a final judgment.

Costs

[59] These are awarded to the plaintiffs on a 2B basis. In the event of any disagreement, memoranda may be filed.

Muir J