IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY

CIV-2013-485-000879
[2013] NZHC 1941

UNDER	the Companies Act 1993
IN THE MATTER OF	the liquidation of Prime Commercial Limited
BETWEEN	CAPITAL CONSTRUCTION LIMITED Plaintiff
AND	PRIME COMMERCIAL LIMITED Defendant

Hearing: 31 July 2013

Counsel: A G Hazelton for Plaintiff
K B Johnston for Defendant

Judgment: 5 August 2013

JUDGMENT OF COLLINS J

Introduction

[1] The question I have to answer is:

> Should Capital Construction Ltd (Capital) be restrained from taking further steps to have Prime Commercial Ltd (Prime) placed into liquidation?

[2] This question raises the following sub-questions:

(1) Can Prime rely on a counterclaim or set-off[1] to prevent Capital from taking further steps to have Prime placed into liquidation?

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[1] A counterclaim usually arises out of a claim that is separate from the debt. A set-off generally arises out of the same transaction as the debt: *Brookers Insolvency Law and Practice* (online [2013]

(2) Should I restrain Capital from continuing with proceeding to place Prime into liquidation because:

(a) Prime says there is a genuine dispute as to whether it owes the money claimed by Capital; and/or

(b) allowing Capital to proceed with its application to have Prime placed into liquidation is oppressive or unfair.

Context

[3] Prime was incorporated in June 1997. Its director is Mr Garnham, who is also a trustee of a shareholder of Prime.

[4] Prime is a commercial property company and the owner of a 15-storey office, car park and residential building in Customhouse Quay called Craig Investment Partners House (the building). In December 2012 the building was valued at $17.45 million.

[5] Capital is a construction company. Its directors are Mr Wickens and Mr Witkowski.

[6] For approximately 12 years Prime and associated companies have engaged Capital to undertake building and renovation work. In February 2010 Prime engaged Capital to undertake earthquake strengthening, reinstatement and refurbishing works in the building. This agreement was not recorded in writing. It is accepted, however, that Capital would render invoices to Prime calculated on the basis of invoices received by Capital from subcontractors and Capital's margin.

[7] From 28 February 2010 to 28 February 2013 Capital rendered invoices to Prime that totalled $1,442,933.50. By 18 April 2013 Prime had paid Capital $960,227.32. Since 1 April 2013 Capital has sent a further four invoices to Prime totalling $32,337.14.

[8] On 10 February 2013 Capital gave Prime notice that it was suspending further work on the building.[2]

[9] On 18 April 2013 Capital issued a statutory demand under s 289 of the Companies Act 1993 in which it sought immediate payment of $482,720.67 being the difference between the total amount of the invoices rendered by Capital to Prime up until 28 February 2013 and the amount paid by Prime to Capital by 18 April 2013. Prime did not pay Capital any of the sum specified in the statutory demand until 26 July 2013.

[10] On 10 May 2013 Prime provided Capital with a payment schedule[3] in which it:

(1)	disputed two invoices totalling	$ 15,750.55;
(2)	disputed it was liable to pay in relation to column strengthening	$ 70,000.00
(3)	said it had been overcharged in relation to seismic strengthening and refurbishment;	$238,000.00
(4)	said it was overcharged in relation to heating, ventilation and air conditioning;	$ 18,750.00
(5)	claimed for loss of rental	$ 51,205.00
	Total	**$393,705.55**

[11] On 20 May 2013 Capital commenced its proceeding to have Prime placed into liquidation.

[12] On 28 May 2013 Prime filed its application for the orders it wishes me to make, namely:

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2 Construction Contracts Act 2002, s 23(2)(b); Affidavit of B Wickens, 26 June 2013 at [46].

3 Construction Contracts Act 2002, s 21(1); First affidavit of M Garnham, 25 May 2013,

(1) An order restraining publication of any advertisement ... or any other information relating to the statement of claim dated 20 May 2013 filed by [Capital] in this proceeding.

(2) An order staying any further proceeding in relation to the liquidation.

[13] Also on 28 May 2013 Prime filed a statement of defence and counterclaim. The counterclaim seeks "$132,333 plus GST in relation to lost rental". Prime has not explained why that sum is significantly different from the loss of rental it claimed in its payment schedule.

[14] On 26 July 2013 Prime:

(1) issued Capital with a notice of adjudication.[4] In that notice Prime said that the disputed sum was $406,338.99;[5]

(2) paid Capital $108,754.33 which Mr Garnham has said was not disputed;[6] and

(3) paid $100,000 into its solicitors' trust account "to be held in escrow in relation to the outstanding disputes".[7]

Can Prime rely on its counterclaim/set-off at this stage in the liquidation process?

Procedure for making and responding to payment claims

[15] The process for making claims for payment in relation to construction contracts, and the process for responding to claims for payment as set out in the Construction Contracts Act 2002 (the Act) was designed "to facilitate prompt and regular payments within the construction industry".[8] The general policy statement in the explanatory note to the Construction Contracts Bill said:

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4 Construction Contracts Act 2002, s 25; Second affidavit of M Garnham, 26 July 2013, Annexure 2MG4.

5 By this time Capital had issued a further invoice for $12,633.44 thereby increasing Capital's claim to $406,338.99.

6 Second affidavit of M Garnham, 26 July 2013 at [26].

7 Second affidavit of M Garnham, 26 July 2013 at [26].

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> Typically, construction industry contracts provide for work to be paid after the work has been carried out. Payments are usually made by instalments as the work progresses, but they are seldom made in advance. This pattern of payment often means that a developer, principal, or head contractor with cash flow problems may deliberately delay payment for work done and, in effect, use those further down the contractual train (for example, sub-contractors) to partially finance the construction project.
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> ...
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> The objective of this Bill is to reform the law relating to construction contracts and, in particular, –
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> - to facilitate regular payments between the parties to a construction contract; and ...
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> ...
>
> - to provide remedies for the recovery of payments under a construction contract.

[16] All of the invoices rendered by Capital to Prime are payment claims under the Act.[9] Accordingly, Prime became liable to pay each invoice 20 working days after each invoice was delivered to Prime.[10]

[17] The consequences of Prime's failure to pay the payment claims include:

(1) The unpaid payment claim becomes a debt due to Capital which it is entitled to recover in any Court.[11]

(2) Capital could suspend work on the building,[12] which it did on 20 February 2013.

Status of counterclaims and set-offs

[18] Section 79 of the Act provides:

> In any proceedings for the recovery of a debt under section 23 or section 24 or section 59, the court must not give effect to any counterclaim, set-off, or cross-demand raised by any party to those proceedings other than a set-off of a liquidated amount if—

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9 Construction Contracts Act 2002, s 20.
10 Section 22(b)(ii).
11 Section 23(2)(a)(i).
12 Section 23(2)(b).

(a) judgment has been entered for that amount; or

(b) there is not in fact any dispute between the parties in relation to the claim for that amount.

[19] It is now settled law that a statutory demand is a proceeding for the recovery of a debt and can therefore not be the subject of a counterclaim, set-off, or cross-demand unless one of the exceptions in s 79 of the Act applies. The reasons for this were explained in *Volcanic Investments Ltd v Dempsey & Wood Civil Contractors Ltd* where Randerson J said:[13]

> Where the debtor is a company, there is nothing in the Act to suggest the issue of a statutory demand under the Companies Act is not a proceeding contemplated by s 79 for recovery of a debt. It is an integral step in the winding up process and is the usual preliminary to a winding-up application under ... the High Court Rules. An application to set aside a statutory demand is a "proceeding" under the High Court Rules. ... An application to wind up a company is also a proceeding under the High Court Rules ... I conclude that recovery of a debt by the lawful process of the issue of a statutory demand and the bringing of winding up proceedings against a debtor company are "proceedings" contemplated by s 79.

[20] If s 79 of the Act applies, then it "trumps" s 290(4)(b) of the Companies Act 1993, which provides a statutory demand may be set aside if:

(b) The company appears to have a counterclaim, set-off, or cross-demand and the amount specified in the demand less the amount of the counterclaim, set-off, or cross-demand is less than the prescribed amount.

The reason why s 79 of the Act may "trump" s 290(4)(b) of the Companies Act 1993 is to give effect to the "pay now, argue later" policy that underpins the Act.[14]

[21] However, in *Laywood v Holmes Construction Wellington Ltd*,[15] the Court of Appeal suggested there may be a distinction between an application to set aside a statutory demand and an application for an order putting a company into liquidation and that s 79 of the Act may not necessarily apply in liquidation hearings. The Court of Appeal deliberately did not rule on this issue but it did say different considerations *may* apply where the Court is asked to order liquidation of a company under s 241 of

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13 *Volcanic Investments Ltd v Dempsey & Wood Civil Contractors Ltd* (2005) 18 PRNZ 97 (HC) at [20].

14 *Gill Construction Co Ltd v Butler* [2010] 2 NZLR 229 (HC) at [9].

15 *Laywood v Holmes Construction Wellington Ltd* [2009] NZCA 25, [2009] 2 NZLR 243

the Companies Act 1993, but up until that point, effect cannot be given to a counterclaim, set-off or cross-demand.

[22] The reason why the Court of Appeal suggested a possible distinction between decisions to liquidate a company and set aside a statutory demand is that liquidation proceedings are primarily designed to enable the collection and distribution of a company's assets among unsecured creditors after payment of preferential debts.[16] For this reason, a decision to liquidate a company may not necessarily be a proceeding for the recovery of a debt.

Does s 79 of the Act apply to Prime's current application?

[23] Prime's claims relating to:

(1) column strengthening;

(2) floor seismic work and refurbishment; and

(3) heating, ventilation and air conditioning

are pleaded as "duplicate costs and/or overcharging"[17] and may therefore be set-offs. Prime's claims relating to lost rental are pleaded as being both a set-off and counterclaim.[18] However, the state of Prime's pleading leaves considerable room for uncertainty about the exact nature of Prime's claims.

[24] Prime argues that for the purposes of s 79 of the Act, its application to prevent the continuation of the liquidation proceeding and the advertising of that proceeding should not be treated in the same way as a statutory demand. Prime says that as the Court of Appeal has left open the possibility that s 79 of the Act does not apply to liquidation orders, I should conclude that s 79 does not apply to Prime's application, on the basis that the considerations that apply to an application for

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16 *Silverpoint International Ltd v Wedding Earthmovers Ltd* HC Auckland CIV-2007-404-104, 30 May 2007 at [79].

17 Statement of Defence and Counterclaim dated 28 May 2013.

18 [illegible]

liquidation orders should equally apply to an application to stay liquidation proceedings.

[25] Like the Court of Appeal in *Laywood* I am deliberately refraining from determining whether s 79 of the Act applies to a decision to liquidate a company. The reason I need not determine that issue is because I am not being asked to decide if Prime should be liquidated. Prime's application asks me to decide if Capital's application to have Prime placed into liquidation should be stayed. In this respect Prime's application equates to a step in the liquidation process.

[26] In my assessment Prime's application to prevent Capital's liquidation proceedings being heard, and to prevent the advertising of those proceedings, should be treated in the same way as an application to set aside a statutory demand. Aside from the public nature of advertising Capital's proceeding, there is no logical distinction between a statutory demand and the steps which Capital needs to take before a Court can consider whether or not to place Prime into liquidation.

[27] The policy behind the "pay now, argue later" regime means that proceedings for the enforcement of an outstanding statutory demand should not be impeded at this stage by an argument that Prime has a counterclaim and/or set-off.

[28] Nothing that I have said should be construed as determining whether or not Prime would be prevented from arguing at a liquidation hearing that it has a valid set-off or counterclaim for the purposes of persuading the Court that the company is able to pay its debts under s 241 of the Companies Act 1993. The extent of my judgment is that s 79 of the Act prevents Prime from arguing at this juncture that Capital's liquidation proceeding cannot proceed to a hearing on the basis of Prime's claim that it has a valid counterclaim and/or set-off.

Should Prime's application be otherwise granted?

[29] Prime's application is made under r 31.11 of the High Court Rules.[19] Therefore Prime's application must be treated as if it were an application for an interim injunction. This in turn requires me to decide whether:

(1) there is a serious question to be tried;

(2) the balance of convenience favours the granting of an injunction; and

(3) the overall justice of the case favours the granting of the relief sought by Prime.[20]

[30] Prime's submissions as to why it says I should grant the orders Prime seeks fall under two headings:

(1) There is a genuine dispute about the outstanding debt.

(2) Capital's proceeding is oppressive and unfair.

Is there a genuine dispute?

[31] Having concluded that, as a matter of law, Prime cannot at this stage argue that it has a counterclaim and/or set-off, it would be surprising if I would nevertheless grant Prime's application to stay the liquidation proceedings on the grounds that there was a genuine dispute in relation to those aspects of Prime's claim that are a counterclaim and/or set-off.

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19 (1) If an application for putting a company into liquidation is made under rule 31.3, the defendant company, or, with the leave of the court, any creditor or shareholder of that company or the Registrar of Companies, may, within 5 working days after the date of the service of the statement of claim on the defendant company, apply to the court—
   (a) for an order restraining publication of an advertisement required by rule 31.9 or any other information relating to that statement of claim; and
   (b) for an order staying any further proceedings in relation to the liquidation.
   (2) The court must treat an application under subclause (1) as if it were an application for an interim injunction and, if it makes the order sought, it may do so on whatever terms the court thinks just.
   (3) The inherent jurisdiction of the court is not limited by this rule.

20 [illegible]

[32] However, in case there is an element of Prime's claim that is not a counterclaim and/or set-off, I will briefly consider whether Prime has established to a sufficient degree that there is a genuine dispute.

[33] In his two affidavits filed on behalf of Prime, Mr Garnham says that Prime disputes that Capital is owed the sum that is sought. In particular, Mr Garnham says:

(1) Capital has overcharged Prime approximately $70,000 in relation to column strengthening work.

(2) Capital has overcharged Prime approximately $238,000 in relation to floor seismic, refurbishment, and reinstatement works.

(3) Capital has overcharged Prime $18,750 in relation to heating, ventilation and air conditioning works.

(4) Capital delayed completing certain work when it placed its resources into another building project in June 2012. As a result Prime says it has not received anticipated rental totalling $51,205.

(5) Capital has sought payment for unnecessary scaffolding costs.

[34] Mr Garnham's reasons for disputing the quantum claimed by Capital are in stark contrast to email exchanges between Mr Garnham and Messrs Wickens and Witkowski from 4 December 2012 to 26 February 2013.[21] In those emails Capital repeatedly sought payment of its invoices. Mr Garnham did not dispute the validity of those invoices. Instead, in his limited responses Mr Garnham recognised Prime's failure to pay the invoices and endeavoured to make reassuring statements to Capital.[22] It is significant that Prime did not raise its arguments about the validity of Capital's claims until after Capital suspended its work on the building.

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21 In particular, I refer to emails from Mr Wickens and Mr Witkowski to Mr Garnham sent on 4 December 2012, 18 December 2012, 19 December 2012, 21 December 2012, 9 January 2013, 5 February 2013, 6 February 2013, 11 February 2013, 15 February 2013, 19 February 2013, 20 February 2013 and 26 February 2013. Affidavit of B Wickens, 26 June 2013, Exhibit 4.

22 In particular, I refer to emails from Mr Garnham to Mr Wickens and Mr Witkowski sent on 19 December 2012, 15 February 2013 and 26 February 2013. Affidavit of B Wickens, 26 June

[35] Furthermore, Prime's claim that it is owed money by Capital is not explained in the detail I expect. Mr Garnham has said Prime is owed approximately $70,000 in relation to column strengthening, approximately $238,000 in relation to floor seismic, refurbishment and reinstatement works and $18,750 in relation to heating, ventilation and air conditioning works. Mr Garnham has not properly explained[23] how those sums are calculated or why he believes there are duplicate invoices. If there was evidence of duplicate invoices that evidence should have been placed before me. Similarly, Mr Garnham has not adequately explained in the detail I expect Prime's claim for alleged losses of rental and why Prime has claimed different sums for rental losses. His evidence that Capital delayed completing certain work when it diverted resources from the building in June 2012 is difficult to reconcile with other evidence that engineering work and consents in relation to that work were not available until 3 September 2012.

[36] For these reasons, I am satisfied Prime has not established the existence of a serious question to be tried in relation to its claims about the sums owed by Prime to Capital. For these same reasons I am not willing to conclude that the overall justice of the case justifies me making the orders Prime seeks on the basis of its claim that there is a genuine dispute. The balance of convenience strongly favours Capital which has had to wait a considerable period to get to the current stage in its efforts to obtain payment.

Is Capital's proceeding oppressive or unfair?

[37] There are six grounds advanced by Prime in support of its submission that Capital's proceeding is oppressive or unfair, namely:

(1) The procedure adopted by Capital is fundamentally unfair.

(2) Prime is solvent.

(3) Prime has provided security.

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[23] Mr Garnham says he could get the work in question completed for a lesser price than charged by

(4) Capital has not been willing to engage with the merits of the parties' dispute.

(5) Prime has commenced adjudication proceedings.

(6) Potential prejudice to third parties.

These factors were advanced on the basis they are factors which weigh in favour of granting Prime's application as part of the overall justice of the case.

Procedure adopted by Capital

[38] Prime says that Capital should have followed "the usual process" of commencing proceedings to have a Court determine the validity of Capital's claim.

[39] I disagree. Capital has relied on the process provided in the Act and Part 16 of the Companies Act 1993. There would be merit in Prime's submission on this point if it could establish the existence of a serious question to be tried in relation to its debt to Capital. It has failed to do so. Accordingly, I conclude there is nothing "fundamentally unfair" about the procedure followed by Capital in this case.

Prime is solvent

[40] Mr Garnham says Prime is solvent. He explained in his affidavits that Prime has obligations to its bank to maintain appropriate loan to value and interest cover ratios and that Prime complies with these obligations and enjoys the support of its bank. Apart from the value of the building, no other information was supplied by Mr Garnham about Prime's solvency.

[41] Mr Garnham's assurances are difficult to reconcile with the acknowledgements he made about Prime's failure to pay invoices rendered by Capital. Prime has failed to produce the evidence I expect it to have produced if it wished to establish that it was solvent.

Prime has provided security

[42] Prime waited until 26 July 2013 to pay the $108,754.33 it says is not disputed and on the same day it decided to pay $100,000 into its own solicitors' trust account as a "buffer"[24] for Capital's claim.

[43] Had Prime seriously wished to convince me it was taking genuine steps to secure Capital's position, then it should have paid the entire sum that Capital is claiming into an independent trust account.

[44] The minimal efforts made by Prime to provide a limited form of security falls well short of the conduct I expect from a company that wishes to persuade me that I should exercise my discretion to prevent Capital carrying on with the next steps in the liquidation process.

Capital is not willing to engage in the merits of Prime's dispute/Prime's referral to adjudication

[45] Prime says that its efforts to have its claims referred to adjudication under the Act have been rebuffed by Capital. Prime also says that it is now a relevant factor that it has invoked the adjudication process under the Act.

[46] It is not surprising that Capital has rejected Prime's suggestion that Prime's claims be referred to adjudication. Prime failed to respond in any meaningful way to Capital's many requests for payment prior to suspension of works on the building. Prime repeatedly failed to honour its promises to pay Capital. Prime's referral of its claim to adjudication now has all the hallmarks of a delaying tactic.

Potential prejudice to third parties

[47] Prime says that allowing Capital to proceed to the next stage in its liquidation proceeding will potentially prejudice third parties. Few details of this alleged prejudice were provided. Mr Garnham says that advertising would create considerable uncertainty for banks in a market which is characterised by building contractors in financial difficulty. It would also limit Prime's ability to employ sub-

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contractors, and would create uncertainty for existing tenants and leasing negotiations.

[48] What is clear is that Capital and its sub-contractors will continue to suffer prejudice unless Prime fulfils its obligation to pay the outstanding invoices immediately and settle its disputes later.

Summary

[49] Prime has failed by a very significant margin to persuade me that the overall justice of the case favours the staying of the liquidation proceeding commenced by Capital. On the contrary, Prime's conduct is a classic example of the type of commercial behaviour that motivated Parliament to pass the Act. Prime appears to have deliberately delayed paying Capital for as long as possible so that those further down the contractual chain effectively financed its construction works. If Prime believes it has a legitimate dispute it should pay now and argue later.

Conclusion

[50] The questions posed in paragraphs [1] and [2] are answered in the following way:

(1) Prime cannot rely on a counterclaim or set-off to prevent Capital from taking further steps to have Prime placed into liquidation.

(2) Capital is not prevented from continuing with its proceeding to have Prime placed into liquidation.

[51] Mr Hazelton, counsel for Capital, suggested that Prime should be given a short period of time to pay the outstanding debt before Capital proceeds to advertise the liquidation proceeding. I have considered whether or not I should issue some form of interim injunction for that limited purpose. However, in my assessment it is better for Capital to decide if it wishes to provide Prime with a short period within which Prime is to pay the outstanding debt.

Costs

[52] Costs should follow the event. In my assessment costs should be awarded to Capital on a scale 2B basis. If the parties disagree then they should file memoranda explaining their positions within ten working days of this judgment. I will deal with any outstanding issue as to costs on the basis of counsel's written submissions.

D B Collins J

Solicitors:
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Stephens Lawyers, Wellington for Defendant