Meltzer Mason Heath
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UPDATE + NEWS + REVIEW

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What a wonderful summer we are having—its hard to remember when we last had one this good! It will be interesting to watch the climate change as we head into Election year 2008.

Directors' Personal Liability – Update
Arron Heath

Readers may recall Rachel Mason's article in the May/June 2007 newsletter commenting on the High Court decision in *Dicks v. Hobson Swan Construction Limited (In Liquidation) and Others*. Readers may also recall that the director of the company was found personally liable in negligence for the loss Mrs Dicks had suffered (based on the fact that he had personally built Mrs Dicks' house).

However, what would be the position where the director of a (development) company did not personally carry out any building work, but did exercise some degree of control over the development? The recent decision of the High Court in *Body Corporate No 188273 v. Leuschke Group Architects Limited* ("the case") has clarified this issue.

Essentially, the High Court held that for a director to be personally liable, he or she must have assumed responsibility for a particular task and been negligent in the undertaking of that task.

The allegation in the case was that the director of the development company had assumed personal responsibility to the (apartment) owners, with the plaintiffs arguing that the development company was simply a vehicle used by the director to isolate himself from personal liability and that he personally was the actual developer. The High Court found that, because there was no evidence the company was a sham, upon its incorporation the development company became the entity which assumed legal responsibility for and controlled all aspects of the development.

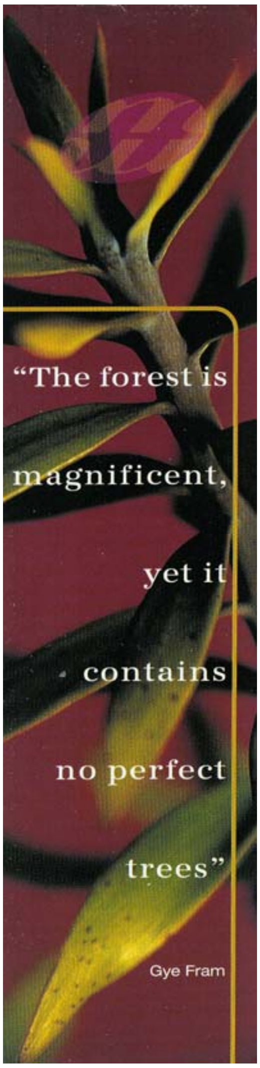
The director never went to the site during construction and gave no direction relating to the design and construction process. The company owned and controlled the development and acted through the agency of its director. The director was entitled to form the company to undertake the development.

The principles set out in *Trevor Ivory Limited v. Anderson* and *Morton v. Douglas Homes Limited* were discussed. The Trevor Ivory case established that the level of control exercised by a director over a particular operation or activity was critical in determining whether a director had assumed responsibility or not. The Morton case had decided that a director's acts or omissions must be directly linked to the defects or damage. Control of a company undertaking a development is not sufficient to establish personal liability in the absence of evidence of an assumption by the director of personal responsibility for defective work.

The judge in the case made the comment that "this result may seem unjust or unfair, but it is the necessary consequence of applying established legal principles. Unless and until Parliament radically reforms the Companies Act 1993, to ensure among other things all companies are capitalised to a level consistent with the financial obligations they assume, similar decisions will be reached".

The case confirmed, at least in the context of leaky building claims, that it is extremely difficult to attribute personal liability to directors of development companies. Control of an area which resulted in defects and proof of negligence is still required.

On the other hand, the principle established in the Dicks' case remains valid, and claims against directors who exercised a high degree of control over the construction process might be more successful.



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Companies Act 1993 Amendments

Rachel Mason

Reporting to Creditors

Two of the amendments to the Companies Act 1993 aim to provide greater accountability of Liquidators to the creditors and shareholders of a company in liquidation. This will be achieved through stricter reporting requirements, as well as enabling a transparency of "who else is affected".

First Reports

Upon commencement of a liquidation, the Liquidator prepares a report on the state of the company's affairs. Previously, there was an exemption available where a distribution to creditors was expected to be less than 20 cents in the dollar. As a matter of practice, we have always prepared such reports, and they are now compulsory in all liquidations.

The major change to the content of the First Report, from our perspective, is an additional requirement contained in section 255(2)(c)(ii)(C). A Liquidator must now send the list of creditors and their addresses (along with the First Report) to the Registrar of Companies, and to all creditors of the company.

Such information forms part of the company's records, may be commercially sensitive, and could have privacy implications. As such, access ought to be limited and was limited by the provisions of section 256. However, legislative policy is to increase the accountability of liquidators to creditors and the objective of requiring a liquidator to send a list of creditors to all creditors is to assist the creditors in organising themselves collectively, presumably with the possible aim of replacing a shareholder appointed liquidator with one nominated by the creditors.

Further reports on the conduct of a liquidation

Section 255(2)(d) states that a Liquidator must prepare a report on the conduct of a liquidation, and proposals for completion, every six months during the course of a liquidation. Previously, there was no requirement to do so if the Liquidator was satisfied there was no likelihood of a distribution to unsecured creditors of any more than 20 cents in the dollar.

That exemption has been repealed, and a Liquidator is now obliged to prepare six-monthly reports for every liquidation, to be sent to every shareholder and creditor, as well as filed with the Registrar of Companies.

While the aim of the legislation is to increase the liquidator's accountability to the creditors, the additional costs of complying with the new requirement will inevitably reduce the funds available for distribution to creditors.

IRD and Current Accounts

Karen Mason

Almost weekly, the IRD are having companies reinstated to the Register and are appointing their preferred Liquidators to recover overdrawn current accounts (and other assets vested in the Crown) from companies that have been removed under section 318 or allowed to lapse causing strike off. The overdrawn current account is then allocated to the shareholders as a salary, and tax calculated on that, which is then payable by the shareholders. Be wary of allowing a client company to be struck off in this manner, as the resultant penalties and interest demanded by the Commissioner can far outweigh the costs of liquidation.

Companies Act 1993 Amendments

Arron Heath

Qualifications of Liquidators

Two further grounds of liquidator disqualification have been added to section 280. The new grounds of disqualification are the provision of professional services by a person or that person's firm or a continuing business relationship with the company, its majority shareholder, any of its directors or any of its secured creditors within the two year period before commencement of the liquidation. The new disqualification grounds do not apply if all the creditors consent to the appointment in question or if the liquidation is solvent.

Between the professional staff at Meltzer Mason Heath there is over 100 years insolvency experience. This means that any problems or uncertainties facing your clients are likely to have been seen by us before. Please call us, and as always we will offer you and/or your clients a free one hour consultation.

Jeff Meltzer, Karen Mason, Arron Heath, Mike Lamacraft, Lloyd Hayward, Rachel Mason, Zané Gouws & Trish McLennan.