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IN THE MATTER OF PRIME VALLEY PROPERTIES LIMITED

SUPREME COURT (Kneller, C.J.): March 16th, 1994

Companies—liquidators—powers and duties—application for directions —liquidator can ask court to determine any question arising in winding up—may grant application on any conditions it thinks just and beneficial

Companies—voluntary winding up—purpose of winding up—improper to pass resolution to pressurize solvent body to pay bona fide disputed debt—improper to use winding-up proceedings instead of common law action

The liquidator of a company applied for directions as to the status of certain sums of money advanced to two of the company's directors.

The company went into voluntary liquidation on August 14th, 1992. N, T and B were all co-directors of the company. N informed the liquidator that before liquidation commenced, the assets not specifically pledged included £4,800 in loans to T and B as advances against profits.

T and B disputed this, claiming that the sums were compensation for the cost of purchasing and running their cars, in default of a company car being provided by N. They claimed that the sums had been termed "advances on profits" in the company accounts for tax avoidance purposes, but it was understood between them and N that this did not reflect the true situation. N denied all knowledge of such an understanding.

The liquidator submitted that there was uncertainty in the company's affairs and that he needed a ruling as to the nature of the £4,800 payment. He therefore took out an originating summons setting out these issues for the court's decision. T and B applied to dismiss the summons.

They submitted that (a) the issue revolved around a disputed debt, a matter which could not be decided in a winding up but rather in a

common law action. An attempt by the liquidator to evade this by seeking directions was an abuse of the process of the court; and (b) it was wrong to use the winding-up process in order to oppress someone who denied a debt, as was being done in this case.

The liquidator submitted in reply that (a) according to the Companies Ordinance, the court had jurisdiction to give the liquidator directions in relation to any matter arising in a winding up; (b) it would be just and beneficial for the court to accede to the application; and (c) as the company was in a voluntary liquidation there could be no question of oppression, and the question to be answered by the court was whether the money received was an advance on profits or a form of compensation.

Held, dismissing the application to set aside the summons for directions:

(1) The court had jurisdiction in a voluntary winding up to give the liquidator directions in relation to any particular matter during the winding up. If the court was satisfied that answering a question would be just and beneficial, it could accede to an application by the liquidator or any aggrieved party under the Companies Ordinance, s.178, wholly or in part, setting out any conditions it thought just. These might include repayments of misapplied funds (page 284, lines 9–22).

(2) The court would not, however, allow a winding up be used to try a common law action or what ought to have been one. Nor would it allow a winding up to be used to put pressure on a solvent body to pay a *bona fide* disputed debt. Neither of these two situations applied in this case, however, and as it was just and beneficial to do so, the application for directions would be allowed (page 284, lines 23–32).

Cases cited:

(1) *Imperial Guardian Life Assur. Socy., In re* (1869), L.R. 9 Eq. 447; 39 L.J. Ch. 147.
(2) *London & Paris Banking Corp., In re* (1874), L.R. 19 Eq. 444.
(3) *National Funds Assur. Co., In re* (1878), 10 Ch. D. 118; 39 L.T. 420.
(4) *Reliance Wholesale (Toys, Fancy Goods & Sports) Ltd., Re, Patterson* v. *Mills* (1979), 76 L.S. Gaz. 731.

Legislation construed:

Companies Ordinance (1984 Edition), s.178: The relevant terms of this section are set out at page 282, lines 20–27.
s.231: The relevant terms of this section are set out at page 282, lines 29–38.
s.252(1): The relevant terms of this sub-section are set out at page 282, line 40 – page 283, line 8.

K. Azopardi for the liquidator;
C. Finch for the directors Mrs. Taylor and Miss Bray;
H.K. Budhrani for the directors Mr. and Mrs. Napoli.

KNELLER, C.J.: Prime Valley Properties Ltd. ("the company") carried on business here as an estate agent that went into what is called a "creditors' voluntary liquidation"—and on August 14th, 1992 its directors and creditors appointed Mr. Lawrence its liquidator.

At that time the co-directors were Mr. Napoli, Mrs. Napoli, Mrs. Taylor and Miss Bray. The shares of the company are held in these proportions: 50% by Prime Valley (International) Ltd.; 25% by Mrs. Taylor; 25% by Miss Bray.

The liquidator studied the company's papers and asked questions of the directors. According to Mr. Napoli, on August 13th, 1992, the day preceding the resolution for the winding up, the assets not specifically pledged included £4,800 in loans to Mrs. Taylor and Miss Bray as advances against profits, so he began to try to recover them.

Miss Bray had written on May 9th, 1990 to Mr. Durante of Durante & Co., the accountants, thanking him for answering her queries that day, and adding:

> "For the sake of good order, I should like to confirm my understanding that the sum of £400 per month, which is being advanced to me by Prime Valley Properties, is not classified as salary for books/taxation purposes. This is an advance (or loan) against prospective profits earned by the company. I understand that it should be paid gross and will not attract taxation until such time as the company's profits (losses!) are subject to tax at the end of the tax year.
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> Please let me know if I have interpreted your advice correctly!"

The next day, Mr. Durante replied by letter that her "interpretation of the proposed loan of £400 per month" was correct. He added this warning:

> "The only comment I would make on this is that if this advance was to continue for a couple of years or so, without the company declaring any dividends, the Commissioner of Income Tax has the right in his discretion to classify this as part of your remuneration and tax you accordingly. At present there is nothing to worry about and if this was to be the case it usually takes two to three years of trading before it comes to light."

The liquidator has a photocopy of a handwritten ledger account of the company showing the payment of £400 a month to each lady as directors' fees and a ledger sheet with £2,400 for each as a shareholder's loan and they are adjustments made by the company's accountant on or after October 31st, 1990.

The liquidator wrote to Miss Bray on August 18th, 1992 telling her she owed the company for—

Share capital unpaid	£25
Cash drawings	£2,400
Total	£2,425

and asking her to send her cheque in settlement within seven days.

On the same day he sent Mrs. Taylor a letter in the same terms. They did not send their cheques or pay those sums in any other way. Mrs. Taylor, it seems, declared she had a counterclaim, so the liquidator asked for full details of it before September 18th, 1992.

Mrs. Taylor and Miss Bray in a joint letter to the liquidator dated September 15th, 1992 wrote in these terms:

> "In January 1990 when the question of salaries was discussed, it was agreed by Francis Napoli, Diana Taylor and Michelle Bray that Diana and Michelle would work on a low salary of £10,000 on the understanding that a company car would be supplied by Francis Napoli for their use. Such vehicle was not forthcoming. Thus Michelle and Diana both bought new cars and it was agreed that an allowance of £400 a month would be paid to each in compensation for buying and using their own cars. This amount was only paid over a six-month period thus:
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> |---|---|
> | D. Taylor | £2,400 |
> | M. Bray | £2,400 |
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> They have not claimed from the company the further five months period for which a company car has not been supplied. Such a claim would amount to an additional £2,000 for each."

The liquidator looked at the management accounts for the period in which the company traded and they did not show any sum for compensation for use of private vehicles but there was a figure of £1,405 for vehicle costs.

Mr. Napoli denied there had been an agreement to provide Mrs. Taylor and/or Miss Bray with a company car or compensation for use of their own vehicles.

Mrs. Taylor and Miss Bray also complained that Prime Valley (International) Ltd.'s management charges of £16,667 were too great, but the liquidator declares that there seems to be little evidence to suggest that these management fees were not agreed from the outset or that any other sum was agreed later or that they are not a liability of the company.

The liquidator discussed all this with Mr. Napoli on November 19th, 1992 and Mrs. Taylor and Miss Bray on January 8th, 1993 but they all maintained their positions on the sums claimed or counterclaimed by them. The ladies said that part of the conversation and agreement to provide them with compensation for the use of their own cars took place before their former legal adviser, Mr. Alfred Vasquez, but he told the liquidator on January 11th, 1993 that he could not recall anything of the sort.

Miss Michelle Pietforte of the company's former accountants wrote to Miss Bray (who passed the letter on to the liquidator on January 2nd, 1993) stating that it was agreed by the directors that moneys were to be paid to Mrs. Taylor and Miss Bray as compensation for the use of their cars.

So the liquidator submits that there is this conflict in the company's state of affairs and he needs an answer to whether the payment of £4,800

was for the use of their private cars by Mrs. Taylor and Miss Bray or directors' fees or a combination of both or a loan repayable by them, and whether the level of management charges should be confirmed. He took out an originating summons on February 3rd, 1993 setting out these issues for the court's determination.

Some time in the middle of May 1993, Mr. Napoli handed the liquidator what seemed to be the cash book of the company and pointed out entries of £400 against the names of Mrs. Taylor and Miss Bray in certain months, described sometimes as advances on profits and sometimes as directors' fees.

Mr. Napoli says the entries are in the hand of Mrs. Diana Taylor and Miss Michelle Pietforte. They reveal that Mrs. Taylor and Miss Bray drew "wages" and, on May 10th and 31st, 1990, £400 each (making a total of £1,600) as an "advance on profit," and then again on June 28th, July 27th, August 29th and September 28th, 1990. Miss Pietforte records the £400 payments each time to Mrs. Taylor and Miss Bray as "directors' fees," although each month they continue to be paid their "wages." He never agreed with Mrs. Taylor or Miss Bray that any payment of £400 to either of them on account of their share of the profits should be treated as directors' fees and he did not tell Miss Pietforte to treat them as such. He maintains that they are accountable to the company for those payments of £400.

Mrs. Taylor's version of the background facts is different. It was agreed between Miss Bray, Mr. Napoli and herself that as directors and sellers of properties the ladies must each have a car. They used their own at their own expense and then it was agreed by all three that Mrs. Taylor and Miss Bray should receive £400 each month from the company to cover the cost of buying their own cars and the depreciation of the cars calculated at 20% a year.

They all wanted to avoid tax on those payments but could not work out immediately how to accomplish this, so for the sake of good order they agreed for bookkeeping purposes to call each one an "advance on profits," but it was understood by them all that that did not reveal the true nature of the payment. Miss Pietforte recognized this and put it in her letter of January 20th, 1993 to the liquidator.

Mrs. Taylor declares that Mr. Napoli's version is a misrepresentation motivated by reasons of personal gain and of considerable animosity towards Miss Bray and herself.

Mr. Napoli's reply is that the accounts prepared by Miss Pietforte for the company which she made available to his solicitor show that she treated the £400 sums paid to them as loans to them as shareholders and there were separate entries for the costs of their motor vehicles.

On June 21st, 1993, Pizzarello, Ag.J. adjourned the liquidator's summons into court for cross-examination of the three directors, Mrs. Taylor, Miss Bray and Mr. Napoli.

When the time came for their cross-examination, however, Mr. Finch for Mrs. Taylor and Miss Bray submitted that the court could not deal with the issue in this form. It was a question of whether the company was the debtor or Mrs. Taylor and Miss Bray were the debtors. There was a disputed debt and that was a matter that could not be decided in a winding up; it had to be resolved in a common law action. This could not be evaded by the liquidator's coming to the court to ask for directions, for that would be an abuse of the process of the court.

Mr. Budhrani, for Mr. Napoli, and Mr. Azopardi, for the liquidator, accepted that it is wrong to file a petition for winding up to oppress someone who denies a debt, but this was not the case here. The company was in voluntary liquidation and the question was whether the £2,400 received by Mrs. Taylor and Miss Bray was payment in advance on account of profits, or repayment of expenses for their use of their cars? The liquidator, having taken the advice of his lawyer, asked the court to decide this. It was the easiest, cheapest, quickest way to solve the matter. The company was not alleging that a third party owed it any sum.

The law cited by the parties is as follows. The Companies Ordinance, s.178 states:

> "(3) The liquidator may apply to the court in manner prescribed for directions in relation to any particular matter arising under the winding up.
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> …
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> (5) If any person is aggrieved by any act or decision of the liquidator, that person may apply to the court, and the court may confirm, reverse or modify the act or decision complained of, and make such order in the premises as it thinks just."

Section 231 states:

> "(1) The liquidator or any contributory or creditor may apply to the court to determine any question arising in the winding up of a company, or to exercise, as respects the enforcing of calls, or any other matter, all or any of the powers which the court might exercise if the company were being wound up by the court.
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> (2) The court, if satisfied that the determination of the question or the required exercise of power will be just and beneficial, may accede wholly or partially to the application on such terms and conditions as it thinks fit, or may make such other order on the application as it thinks just."

Section 252(1) states:

> "If in the course of winding up a company it appears that any person who has taken part in the formation or promotion of the company, or any past or present director, manager or liquidator, or any officer of the company, has misapplied or retained or become liable or accountable for any money or property of the company, or been guilty of any misfeasance or breach of trust in relation to the

company, the court may, on the application of the official receiver, or of the liquidator, or of any creditor or contributory, examine into the conduct of the promoter, director, manager, liquidator or officer, and compel him to repay or restore the money or property or any part thereof respectively with interest at such rate as the court thinks just, or to contribute such sum to the assets of the company by way of compensation in respect of the misapplication, retainer, misfeasance or breach of trust as the court thinks just."

This is in the same terms as s.165 of the Companies Act 1862.

A winding-up petition is not to be used as machinery for trying a common law action. This is exemplified in *In re Imperial Guardian Life Assur. Socy.* (1) (L.R. 9 Eq. at 450, *per* James, V.-C). In that case claimants against an assurance company in respect of a disputed policy brought an action and the company went into voluntary liquidation. The claimants petitioned for the compulsory winding up of the company, and a month later the voluntary liquidators offered to hold themselves personally liable to pay the claimants whatever might be found due to them in the action and to set aside out of the assets a sum sufficient to meet the claim (if it should be established) with interests and costs. The court held that the petition would be stood over until after the trial of the action, the liquidator's undertaking would be extended, and the claimants were ordered to pay all the costs incurred since the liquidator's offer.

Where a creditor whose debt is *bona fide* disputed serves a statutory notice requiring payment of that debt by a company within three weeks, and there is no evidence of the insolvency of the company (other than non-compliance with the notice) and it denies insolvency, the creditor's petition will be dismissed with costs if the circumstances show in the opinion of the court that the petition is not to obtain a winding-up order, but to put pressure on the company (*In re London & Paris Banking Corp.* (2)).

The liquidator of a limited company in the course of being wound up could apply to the court under s.165 of the Companies Act 1862, to compel a director to repay moneys of the company misapplied by him. The creditors of the company were entitled, according to their contract with the company, to have its capital reserved for payment of their claims (*In re National Funds Assur. Co.* (3) (10 Ch. D. at 121)).

The liquidator has a duty to collect the assets of the company and they include the company's moneys misapplied or wrongfully retained by an officer of the company (*Re Reliance Wholesale (Toys, Fancy Goods & Sports) Ltd., Patterson* v. *Mills* (4)). This company owed a director £7,500 on terms that he should be repaid when the company could afford to do so. He found at the office blank cheques signed by a co-director. He filled in one made out to himself for £5,500 which was still owing to him and counter-signed it. He paid it into his account though his co-director told him not to do so and it was met. The company went into voluntary liquidation and the liquidator took out a summons asking for directions.

The judge found the director guilty of misfeasance and ordered him to repay the £5,500 to the liquidator for the company and the Court of Appeal affirmed the judgment. The co-director had objected to repaying that sum at that juncture so the company could not be said to intend to repay then. A counterclaim against the company by the director would have failed as the company could not afford to repay him. The director could not apply for a set-off when he was guilty of misfeasance. See also *Palmer's Company Law*, 24th ed., paras. 88–89, at 1474 (1987).

On the papers and submission of counsel, applying the law to the facts, I make these observations. According to the Ordinance, this court has jurisdiction in a voluntary winding up to give the liquidator directions in relation to any particular matter during the winding up. It can also confirm, reverse or modify an act or decision of his if anyone complains of it and, if necessary, make such order as it thinks just. The liquidator or any contributory or creditor can ask the court to determine any question arising in the winding up and, if satisfied that answering the question will be just and beneficial, the court may accede to the application wholly or in part and, if necessary, set out such terms and conditions and orders as it thinks just. It can compel a director or officer of the company to repay or restore the company's moneys that he has misapplied or wrongly retained. The liquidator has his duty to collect the company's assets and the court has this jurisdiction and these powers to help him do so.

The court will not, however, let a winding up be used for trying a common law action or what ought to be one.

Here, in this voluntary winding up, no common law action has been launched. The resolution to wind up was not passed to put pressure on someone who is solvent to pay a *bona fide* disputed debt.

The liquidator, on legal advice, has asked the court to determine questions which have arisen in the winding up and since it will clearly be just and beneficial I accede to his application. The application of counsel for Mr. Taylor and Miss Bray to dismiss the summons with costs is denied.

Order accordingly.
