IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2014-404-001661
[2014] NZHC 2504

UNDER	The Companies Act 1993
IN THE MATTER	of the liquidation of Doyle By Design Limited (in Liquidation)
BETWEEN	DAMIEN GRANT and STEVEN KHOV Applicants
AND	BB2 HOLDINGS LIMITED Respondent

Hearing: 6 October 2014

Appearances: A Ho and A Cherkashina for Applicants
J E M Lethbridge for Respondent

Judgment: 6 October 2014

ORAL JUDGMENT OF ASSOCIATE JUDGE R M BELL

Solicitors: Waterstone Insolvency, Auckland
Grove Darlow & Partners, Auckland

Introduction

[1] This is a voidable transaction case. The liquidators of Doyle By Design Limited (in liquidation) claim $42,720.78 from the respondent.

[2] The company law reforms in the 1990s abandoned the test for preferences based on intention in favour of an effects-based test.[1] Under the Companies Amendment Act 2006, the defence that payments were made in the ordinary course of business was removed.[2] These changes have widened the scope of the law relating to voidable transactions. They have allowed liquidators to challenge a far greater range of transactions between insolvent companies and their creditors. Adventurous liquidators continue to probe the outer reaches of the changes made in the law. Quite some time ago I gave up the idea that there were no new questions in voidable transactions.

[3] In this case the liquidators are challenging payments made to a secured creditor. Subject to one matter I will need to discuss further, they do not challenge the security. They accept that it was valid and enforceable and do not apply to set it aside. They say however that in the circumstances of this case they are entitled to disregard the security.

[4] It will be necessary to set out their argument more fully, but the ultimate effect of it is that the payments the company made to the respondent can be treated as payments to an unsecured creditor, and are therefore recoverable because the company was at all material times insolvent, and the respondent has received more than will be available to unsecured creditors in the liquidation.

[5] The applicants are the current liquidators of Doyle By Design Limited. The director of Doyle By Design is a Mr Craig Doyle. The respondent's name is BB2 Holdings Limited, but at the times relevant to this proceeding it carried on business under a different name, Blackbird Finance Limited.[3] I will refer to the respondent as Blackbird.

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1 Companies Amendment Act 1993, s 41; Companies Act 1993, ss 292-296.

2 Companies Amendment Act 2006, s 27.

3 It changed its name when it sold its business to a new company now called Blackbird Finance Limited. For this proceeding that change of ownership is irrelevant.

Some facts

[6] In February 2008 Blackbird sold computer hardware and software to Doyle By Design. The items are described as Tharsten SQL printer management information system software, a web server, and an SQL server. That was a credit sale agreement under which Blackbird retained title in the equipment until it was paid in full. Blackbird registered its security interest under the Personal Property Securities Act 1999. The purchase price was $88,780.65. Doyle By Design was required to make an initial payment of $2,730.46 and a second payment a month later of $8,231.78. Afterwards it was to pay monthly instalments of $1,365.23 over 56 months. Doyle By Design was occasionally late in making monthly instalments, but those defaults were apparently remedied within short time. That changed in January 2010, when Doyle By Design again defaulted. This time Blackbird made enquiries and found out that Mr Doyle had gone to Queensland without any intention of returning and he had effectively abandoned the business. Blackbird gave notice under s 128 of the Property Law Act 2007 and repossessed the assets on 10 February 2010.

[7] Mr Doyle and the trustees of his family trust had given guarantees under the credit sale agreement. Even though he had abandoned the company in New Zealand, Mr Doyle was still keen to carry on business in Queensland. For that he saw benefit in being able to use the equipment seized by Blackbird. For its part Blackbird was looking to Mr Doyle as guarantor to honour his obligations under the credit sale agreement. Blackbird and Mr Doyle made an arrangement. Mr Doyle would give Blackbird security by way of a mortgage over an apartment he still owned in Normanby Road, Mt Eden, Auckland; Blackbird would let him have the equipment; Mr Doyle would continue to pay the instalments under the credit sale agreement. Apparently he has continued to make those payments.

[8] On 16 April 2010 an application was made for Doyle By Design to be put into liquidation. That means that the specified period under s 292(5) of the Companies Act began on 16 April 2008. The restricted period under s 292(6) began on 16 October 2009.

The payments challenged under s 292

[9] In their application the liquidators seek orders setting aside payments of instalments to Blackbird within the specified period. The total is $42,720.78. The first payment was made on 21 April 2008 and the last one on 19 April 2010. The payments during 2010 total $6,876.15. They were all made during the restricted period and after Blackbird had taken possession of the equipment.

Issues

[10] The issues in the case are these:

(a) Was Doyle By Design unable to pay its debts at the time of the payments?

(b) Did Blackbird receive more than it would in the liquidation? Here, the primary issue is how the Court should deal with the security that Blackbird held under its credit sale agreement.

(c) Does Blackbird have a defence under s 296(3) Companies Act?

Objection to reply affidavit

[11] Before I consider those main issues, there are two preliminary matters to be addressed. Ms Lethbridge objected to the liquidators' reply affidavit. She submitted that that affidavit contained passages that were irrelevant, amounted to inexpert opinion, submissions on law and were argumentative in content. She referred to McGechan J's decision in *Donovan v Graham*.[4] That was a case where one party applied to strike out parts of an affidavit ahead of the trial. McGechan J noted, however, that the more usual situation is one where the judge picks his way through the total material at ultimate trial stage, discarding the dross.[5] He also commented:[6]

> Evidential dogma should not impede sensible resolution in a Judge-alone trial of this character.

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4 *Donovan v Graham* (1991) 4 PRNZ 311 (HC).
5 At 313.
6 At 314.

[12] In this case I do not discard the reply affidavit in its entirety. There are passages that are unacceptable as amounting to argument, irrelevancy, inexpert opinion, and submission, but I can read the affidavit while attaching no weight at all to those passages. I do not need to make any formal strike-out rulings for particular passages in that affidavit. I have been able to deal with the issues unswayed by the dross.

Multiple notices under s 294

[13] The second preliminary matter is a point raised in the notice of opposition to the application but not sustained in the hearing. The point is that the liquidators issued three notices under s 294 Companies Act. The argument signalled in Blackbird's notice of opposition was that having issued one notice, it was not open to liquidators to give a fresh one.

[14] The notices in question were these:

(a) A notice of 13 May 2011 putting in issue payments amounting to $32,146.92 made between May 2009 and April 2010.

(b) A notice issued in May 2012 setting aside payments totalling $56,573.32 between April 2008 and April 2011. That included payments made after the start of the liquidation.

(c) A notice of 22 July 2013, the one in issue in this case, for payments made between April 2008 and May 2010, totalling $42,720.78.

[15] In the hearing Ms Lethbridge did not submit that the final notice was invalid. That was a responsible concession. In my view it was open to the liquidators to issue one notice and later, having reassessed the matter and deciding that they wanted to take more transactions, to issue a fresh notice to show clearly to the respondent that a wider range of payments was now in issue. The liquidators accepted the point that it was not open to them to attack payments made to the respondent after liquidation. They issued a fresh notice leaving transactions after liquidation out of account. That was responsible because that ensured that the notice focused only on payments truly at issue.

[16] Just as a party in a proceeding may amend their pleadings as the case progresses, often in the light of a fresh evaluation of the case, it seems to me also open to liquidators to issue new notices if they consider that in the light of fresh considerations the transactions to be attacked ought to be either expanded or narrowed. So long as they keep within the six-year limitation period I see no objection to the liquidators having issued three notices in this case.

Was Doyle By Design unable to pay its debts at the time of the payments?

[17] Blackbird did not strongly contest the issue of insolvency. Nevertheless the liquidators are still required to show that Doyle By Design was unable to pay its debts during the period of the transactions.

[18] It is abundantly clear that by January 2010 Doyle By Design was insolvent. Blackbird acknowledges that. There is also good evidence that Doyle By Design was insolvent at least from March 2009. The liquidators established that by reference to the claims made by unsecured creditors. There are undisputed debts going back to March 2009. One creditor, the Commissioner of Inland Revenue, has a debt for income tax going back earlier than that. That is for a relatively small sum, and by itself does not prove inability to pay debts earlier than 2009.

[19] To cover the earlier period (from April 2008 to March 2009), the liquidators have relied on balance sheets of Doyle By Design. These are management accounts. There is no sign that they have been prepared by an independent chartered accountant. While they are hearsay statements, they are business records within s 19 of the Evidence Act 2006 and are therefore admissible.

[20] There are some signs of amateurishness in the balance sheet. There appears to be no attempt to distinguish between current liabilities and term liabilities: all liabilities are treated as current, even the Blackbird debt, which was payable over some 56 months.

[21] The 2009 balance sheet shows the financial position of the company from month to month from April 2008 onwards. While there may be some misgivings about these management accounts, the position is tolerably clear that throughout

Doyle By Design was not able to pay its debts as they fell due. The primary evidence supporting that is the net asset position which was almost entirely negative throughout that period. It is therefore unnecessary to examine the cash flow position, the difference between current assets and current liabilities. I accept that during 2008 and the early part of 2009 Doyle By Design was not able to pay its liabilities as they fell due. In taking this approach, I follow the principles set out by Richardson J in *Re Northridge Properties Limited.*[7] His judgment on the question of ability to pay debts has been cited again and again in this context.

Has Blackbird received more towards satisfaction of its debt than it would likely receive in the liquidation?

[22] The main question here is Blackbird's status as a secured creditor. Before I deal with that, I make two preliminary comments. The first is that when a question arises under s 292(2)(b), the onus is on the liquidators to show that the creditor has received more than it would in the liquidation.

[23] The second goes to what provision there will be for creditors in the liquidation. To establish that there has been a preference, there needs to be a comparison between what the alleged preferred creditor has received and what other creditors are likely to receive in the liquidation. That comparison cannot be made if the position of unsecured creditors is not set out in the evidence. The liquidators' affidavit does not expressly address that question. However, in the hearing, Mr Ho was able to refer to the financial statements for the year ending 31 March 2010 to satisfy me that it was possible to infer that the unsecured creditors in this liquidation would not be able to receive as much as was paid to Blackbird.

[24] The financial statements show the balance sheet for February 2010. I bear in mind that at that stage the company had ceased business, and no business would have been carried on between February 2010 and the date of the liquidation order. The balance sheet shows assets of $48,000 and total liabilities of $376,000, a net deficiency of $328,000. In other words, assets of approximately $48,000 may be available for creditors claiming $376,000.

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7 *Re Northridge Properties Limited (in liq)* SC Auckland M 46/75, 13 December 1977.

[25] I am satisfied that if Blackbird is an unsecured creditor it has received more than would be available to unsecured creditors generally. I bear in mind of course that the unsecured creditors would not receive a pari passu distribution of the entire $48,000. Before any of that could be paid to them, there will be the costs of realisation, the costs of liquidation, and there is also part of the debt to the Commissioner of Inland Revenue, a preferential creditor.

[26] That brings me to Blackbird's security. At the outset I said that the liquidators generally did not challenge the validity of the security. They raised one small point. That was that the assets which were the subject of registration under the Personal Property Securities Act were not all the assets in the credit sale agreement.

[27] Ms Lethbridge effectively answered that point. She demonstrated by reference to the documents that the words used in the financing statement could be considered a global description of all the assets sold under the credit sale agreement. In any event, for this case it would not matter whether there had been a valid registration under the Personal Property Securities Act. I am concerned only with the validity of the security as between the company and Blackbird. I am not required to consider rights of third parties.[8]

[28] The argument for the liquidators that they are entitled to attack the payments made to Blackbird runs generally as follows. They refer to the definition of a security interest in s 17 of the Personal Property Securities Act.

> **Meaning of security interest**
>
> (1) In this Act, unless the context otherwise requires, the term **security interest**—
>
> (a) means an interest in personal property created or provided for by a transaction that in substance secures payment or performance of an obligation, without regard to—
>
> > (i) the form of the transaction; and
> >
> > (ii) the identity of the person who has title to the collateral; and

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[8] Personal Property Securities Act, s 36 and see *Dunphy v Sleepyhead Manufacturing Co Ltd* [2007] NZCA 241, [2007] 3 NZLR 602 at [6].

(b) includes an interest created or provided for by a transfer of an account receivable or chattel paper, a lease for a term of more than 1 year, and a commercial consignment (whether or not the transfer, lease, or consignment secures payment or performance of an obligation).

(2) A person who is obligated under an account receivable may take a security interest in the account receivable under which that person is obligated.

(3) Without limiting subsection (1), and to avoid doubt, this Act applies to a fixed charge, floating charge, chattel mortgage, conditional sale agreement (including an agreement to sell subject to retention of title), hire purchase agreement, pledge, security trust deed, trust receipt, consignment, lease, an assignment, or a flawed asset arrangement, that secures payment or performance of an obligation.

[29] They point out that while Blackbird holds a perfected purchase money security interest, its rights are defined by the Personal Property Securities Act and limited to the rights in that Act. That entitles Blackbird to the actual equipment and to the proceeds of the equipment under s 45 of the Act.[9]

[30] After Blackbird took possession of the equipment, it allowed Mr Doyle to take it. In these circumstances Blackbird does not have any right to the equipment, and has not received the proceeds of any disposition of the equipment. Therefore any funds it has received must have come to it as an unsecured creditor. They say that as Blackbird has been paid as an unsecured creditor, those payments can be attacked under s 292.

[31] Blackbird's position is directly to the contrary. While Ms Lethbridge did not state the matter quite as bluntly, the general tenor of her submission was, "Once a secured creditor, always a secured creditor". Her submissions were along the lines that a secured creditor stood outside the liquidation provisions of the Companies Act. She referred to the provisions for secured creditors under s 305 and pointed out that

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[9] Personal Property Securities Act, s 45:

Continuation of security interests in proceeds

(1) Except as otherwise provided in this Act, a security interest in collateral that is dealt with or otherwise gives rise to proceeds—

(a) continues in the collateral, unless the secured party expressly or impliedly authorised the dealing; and

(b) extends to the proceeds.

(2) The amount secured by a security interest in collateral and the proceeds is limited to the value of the collateral at the date of the dealing that gave rise to the proceeds, if the secured party enforces the security interest against both the collateral and the proceeds.

Blackbird had not made a claim in the liquidation. She referred to s 312 and the provision that assets available for distribution are not to include assets subject to a charge. I note also, while she did not refer to it expressly, that the definition of "creditor" under s 240 Companies Act excludes secured creditors except in defined cases, and the special cases do not apply here.

[32] More importantly, she also referred to a passage from Heath & Whale's *Insolvency Law in New Zealand*:[10]

> The statutory order of priority will generally be disturbed if an unsecured creditor receives full payment of its debt during the specified period when the company is insolvent. However a payment made to a secured creditor will generally not be impugnable by the liquidator as such payment does not affect the position *vis-à-vis* the other creditors in the liquidation. Accordingly a payment made to a secured creditor, or to an unsecured creditor that enjoys priority over the general body of unsecured creditors, will rarely be able to be impugned as the effect of the transaction does not result in the creditor receiving more than it is entitled to in the liquidation. A preference may result, however, if the order of payment is deferred.

[33] Blackbird relies on that to say that by virtue of its status as a secured creditor, the payments it received are immune from attack under s 292.

[34] In my view the arguments for both sides go too far. It may be helpful to go back to some first principles. In referring to a "secured creditor" I mean someone who has taken a charge over assets of a company. I use "charge" as it is defined in s 2 of the Companies Act.[11]

[35] Being a secured creditor entails the following. A secured creditor is entitled to look to a company for the performance of an obligation, typically payment of money. In addition, a secured creditor takes an interest over an asset or assets of the company by way of security for performance of the obligation. That entitles the creditor to take enforcement steps in relation to that asset when the instrument creating the interest so allows, usually upon default.

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[10] Paul Heath & Mike Whale *Insolvency Law in New Zealand* (2nd ed, Lexis Nexis NZ Ltd, Wellington, 2014) at [20.23(b)]; also in the online loose-leaf ed, Lexis Nexis at [24.50(b)].

[11] **Charge** includes a right or interest in relation to property owned by a company, by virtue of which a creditor of the company is entitled to claim payment in priority to creditors entitled to be paid under section 313; but does not include a charge under a charging order issued by a court in favour of a judgment creditor.

[36] It is important to note the relevance of the value of the asset in relation to the debt payable to the creditor. Prudent secured creditors ensure that the asset over which they take security has sufficient value that if they need to take enforcement steps they can be paid in full out of the proceeds of sale. Those are fully secured creditors. It can happen, however, that the value of the asset is not enough to meet the entire debt payable to the secured creditor. In that situation the creditor is partly secured. When the creditor has security for only part of its debt, it is to a certain extent unsecured.

[37] The approach of the Companies Act is that secured creditors are in a preferred position. Their right to look to the assets of the company is preserved when a company goes into liquidation. There is a helpful explanation of the policy underlying that approach in Professor Goode's text, *Principles of Corporate Insolvency Law.*[12] There he says:[13]

> … we can see that the protection of ownership and security interests rests on sound principles. Rights of ownership should in principle be respected, for if they are not upheld on insolvency the distinction between property and obligation becomes largely meaningless. The same is true of security interests. To deny recognition of the secured creditor's real rights upon the debtor's insolvency would be to use the very event against which the security interest was designed to give protection as to the ground for its destruction. The economic justification for upholding security rights was well put by Professors Jackson and Kronman in a much-cited article published 26 years ago:
>
> > "…if the law denied debtors the power to prefer some creditors over others through a system of security agreements, a similar network of priority relationships could be expected to emerge by consensual arrangement between creditors. Permitting debtors to encumber their assets achieves the same result, but in a simpler and more economical fashion. If a debtor has more than two or three creditors, free-rider and holdout difficulties are likely to plague any attempt on the part of creditors to work out a set of priority relationships among themselves. These transaction costs can be avoided by allowing the debtor himself to prefer one creditor over another. The rule permitting debtors to encumber their assets by private agreement is therefore justifiable as a cost-saving device that makes it easier and cheaper for the debtor's creditors to do what they would do in any case."

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[12] Roy Goode *Principles of Corporate Insolvency Law,* (4th ed, Sweet & Maxwell, London, 2011).

[13] At [2-29].

> In policy terms, the secured creditor is accorded priority because he bargained for it; other creditors who chose to lend unsecured cannot complain of their subordinated position.

[38] Later in his text Professor Goode considers the question of preferences in payments to secured creditors. That part of his text is more extensive than the passage in Heath & Whale that Blackbird relies on.[14] He says:[15]

> In general, payment to a secured creditor in reduction or discharge of the debt is not a preference, for the effect of the payment is to reduce or extinguish the security interest and thus *pro tanto* to increase the company's equity in the previously charged assets and make them available to other creditors. Accordingly, the payment produces no change in the value of the assets available for the general body of creditors. Moreover, if the company were to refrain from making the payment, that would not help the other creditors, for the secured creditor would still be entitled to enforce his security, assuming the giving of it had not itself been by way of preference.

[39] Having stated that general position Professor Goode notes that there are exceptions. Some of the exceptions he refers to are relevant only to English law - for example, those arising under floating charges, which have now disappeared from New Zealand law as a result of the Personal Property Securities Act. But one exception is this:

> …where the amount of the payment exceeds the value of the security; in that event, the payment is vulnerable to the extent of the excess.

[40] In my view, the question in this case lies within that situation noted by Professor Goode as an exception to the general principle. One matter that comes out of Professor Goode's analysis is that so long as the value of the asset taken as security is worth more than the debt payable by the company there can be no element of preference. Payments made to a secured creditor will either reduce the debt or prevent the debt increasing on account of additional interest arising upon default. On payment made to a fully secured creditor, any equity left is available for unsecured creditors. Unsecured creditors benefit from the debt to the secured creditor being paid but they suffer if the debt is not paid because the equity available

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[14] Andrew R Keay *McPherson's Law of Company Liquidation* (3rd ed, Sweet & Maxwell, London, 2013) at [11-064] also says: "It is well settled that a payment in discharge of a valid security cannot constitute a preference." *National Australia Bank Ltd v KDS Construction Services Pty Ltd* (1987) 163 CLR 668 (HCA) at 679 is cited.

[15] At [13-93].

to them will be reduced by reason of the corresponding increase in the debt, the subject of the security.

[41] What Professor Goode does not discuss in detail is the position of payments to a partly secured creditor. The approach I take is that when a creditor is partly secured, any payments it receives go first to reduce the *unsecured* part of the debt. Take the case of a partly secured mortgagee of land – a common figure in summary judgment applications. A mortgagee who has suffered a shortfall in a mortgagee sale is a partly-secured creditor. Payments received from the mortgagor up until the date of sale are applied to pay down the unsecured part of its debt. This means that the full extent of the security is available to the mortgagee when receiving the proceeds of any sale. That is an application of s 185 of the Property Law Act, but it seems to me that the principle is no different when the asset the subject of the security is personal property rather than land. It would be absurd and contrary to normal commercial practice for a partly secured creditor to treat its security as reduced on a payment by the debtor company. Only when the unsecured portion of the debt is discharged are payments applied to reduce secured debts.

[42] It is therefore necessary to consider whether Blackbird received the payments as a wholly secured or a partly secured creditor. If, as Blackbird maintains, it was at all material times wholly secured, there can be no element of preference under Professor Goode's approach. On the other hand, if Blackbird was partly secured when it received payments, those payments went first towards the unsecured portion of the debt and could not go to the secured part of the debt.

[43] Was Blackbird a fully secured creditor or a partly secured creditor? There is clear evidence that by early 2010 Blackbird itself recognised that it was at least, to some extent, unsecured. That appears in the evidence of Mr Laird, a director of Blackbird, describing the discussions with Mr Doyle in early 2010:

> Mr Doyle told BFL that the computer and software were very important to the running of his design business in Australia, as they previously had been for the New Zealand business. He was able to convince BFL that allowing him to continue using the assets would give us a far better chance of getting its money back than any attempt to sell them on the open market – this has certainly proved to be the case.

[44] That is recognition that the equipment was not worth enough to cover its debt in full. I take that as clear evidence that Blackbird was partially unsecured at that time. It therefore received payments as an unsecured creditor in 2010. In fact the bank statements put in evidence by the liquidators show that another creditor, ANZ Bank, financed those payments. At the start of 2010 Doyle By Design's account with the ANZ Bank was marginally in credit, and by the date of liquidation it was in overdraft to the sum of about $13,000. Drawings against its account allowed Blackbird to receive the payments.

[45] The payments made during this period were $6,876.15. I find that Blackbird received them as an unsecured creditor, and they were more than it would have received in the actual liquidation.

[46] That deals with only some of the payments the subject of the liquidators' claim. The next question is whether the liquidators are able to attack the earlier payments to Blackbird, the $35,844.63 paid before January 2010.

[47] The question here is whether Blackbird was fully secured at the time each payment was made. It is important that I put this into proper context. This is not a case where the secured creditor has been paid in full so that the asset has been released and is available for unsecured creditors generally. Nor is it a case where there has been a default leading to the secured creditor selling up the asset so that the shortfall can be identified. This is a somewhat anomalous in-between position where the asset has been seized, but it has not been sold. The process of enforcement has not been carried through.

[48] In my view it needs to be shown that when the payments were made to Blackbird up until the end of 2009, Blackbird was not fully secured for its debt. That requires evidence as to the value of the security during 2008 and 2009. While I have been able to refer to Mr Laird's evidence to infer that the security was obviously not good enough in early 2010, I am not able to draw any such inference for any earlier period. It would be necessary for the liquidators, who have the burden of proof, to adduce evidence that when payments were made to Blackbird, Blackbird was unsecured rather than fully secured.

[49] Mr Ho makes the point that the equipment in the agreement for sale and purchase would depreciate. While I can understand as a general proposition that it would depreciate, there is not enough evidence to know the appropriate rate of depreciation to apply and how the depreciation rate would apply against the amount of the debt. In this situation it is speculative for me to hold that perhaps at some period before the end of 2009 Blackbird was unsecured. I bear in mind that the onus is on the liquidators and they have not shown that to be the case.

[50] I come back to the submissions for Blackbird. Its case is that it is entitled to rely on s 305 of the Companies Act and stand outside the liquidation. In its view the question of being partly unsecured is totally irrelevant. It is entitled to choose which course to take under s 305(1):

> **Rights and duties of secured creditors**
>
> (1) A secured creditor may—
>
> (a) realise property subject to a charge, if entitled to do so; or
>
> (b) value the property subject to the charge and claim in the liquidation as an unsecured creditor for the balance due, if any; or
>
> (c) surrender the charge to the liquidator for the general benefit of creditors and claim in the liquidation as an unsecured creditor for the whole debt.

[51] In my view, nothing in s 305, nor for that matter s 312, stands in the way of a liquidator assessing whether a creditor is secured or not, and, if the creditor is unsecured for part of the debt, then deciding whether payments made to that creditor are voidable under s 292. The arguments by Blackbird that s 305 gives it a defence, in my view, do not prevail.

[52] To summarise on the question of preference, I have found that payments made during 2010 are voidable under s 292. I have been unable on the evidence to find that payments made to Blackbird before 2010 were voidable as it is not clear whether Blackbird received them as a fully secured creditor or only as a partly secured creditor.

Does Blackbird have a defence under s 296(3)?

[53] In her oral submissions, Ms Lethbridge made it clear that Blackbird was relying on s 296(3) only for payments made up to the end of 2009. She accepted that in early 2010 Blackbird had clear knowledge of the actual insolvency of Doyle By Design and therefore it could not rely on the defence for the payments made in 2010. Her arguments as to s 296(3) were a backup defence, in case Blackbird's argument as to preference did not apply to the payments in 2008 and 2009. Because I have found in favour of Blackbird already in this respect, it is unnecessary for me to spend a much time on the defence under s 296(3). I will state my conclusions briefly.

[54] I generally accept the tenor of the evidence of Mr Laird, director of Blackbird. I make a finding of good faith in favour of Blackbird under s 296(3)(a). I bear in mind that the question of good faith goes to honesty of belief rather than reasonableness of belief. There is nothing in the evidence to suggest that Blackbird acted in anything but in good faith.

[55] I accept that up until the end of 2009 Blackbird did not have enough information to give rise to suspicion under s 296(3)(b). The liquidators noted that there had been, in some cases, delays in payments with defaults remedied. I accept the explanation of Mr Laird that they were not out of the ordinary at that time, particularly in Blackbird's experience as a second-tier lender. The fact that payments were not always made on time and that there was an occasional delay in payment does not, by itself, trigger a suspicion of an inability to pay debts. I bear in mind, in particular, that when there were missed payments, the defaults were quickly remedied. That might suggest temporary cash flow difficulties to a secured creditor but would not make it suspect insolvency.

[56] However, I find against Blackbird on change of position under s 296(3)(c). Initially it was suggested that there had been a change of position by the action taken after the equipment was repossessed. That was action taken by an unpaid creditor who looks to its security and its guarantors to redress the non-payment of its debt. That ordinary recovery action does not, in my view, amount to action in reliance of the validity of the payments made earlier.

[57] Taking another tack, Ms Lethbridge submitted that there was deliberate conduct by Blackbird in refraining from taking any enforcement action in reliance on the validity of payments during 2008 and 2009. The submission ran that if Blackbird had known the true financial position of Doyle By Design, it could have taken earlier action. It has suffered a detriment by not being able to do so.

[58] I do not accept that argument. Because there had not been any relevant defaults to the knowledge of Blackbird during 2008 and 2009, Blackbird was unable to take any enforcement action anyway. Specifically any delays in payment were quickly remedied and Blackbird did not have any relevant knowledge of Doyle By Design's insolvency during those two years. It was constrained by its contract and by the general law[16] from taking any enforcement action during that period. It cannot say that its failure to take enforcement action was a deliberate omission on its part.

[59] I therefore reject the defence under s 296(3).

Conclusion

[60] I find that Blackbird should pay the liquidators $6,876.15. There is, however, the matter of costs. In September 2012 Blackbird offered to pay the liquidators that very sum. It made that offer in an open letter. That was a tender of the debt before the proceeding started. In those circumstances, a defendant liable for the debt which it said it was ready to pay before the proceeding started should not be ordered to pay costs.[17]

[61] Mr Ho wanted the opportunity to file further written submissions on costs. In my view, that is unnecessary. Where a person in the position of a defendant has tendered payment in an open letter before the proceeding, and the plaintiff recovers no more than amount of that offer, the defendant should have the costs of the proceeding, having been put to the trouble of unnecessarily defending the proceeding.

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16 For example the restriction on repossession and acceleration under s 128 of the Property Law Act.

17 See for example *Griffiths v School Board of Ystradyfodwg* (1890) 24 QBD 307 (CA).

[62] There is no basis for any increased costs or for reduced costs. I order costs under category 2 band B for this proceeding. If the parties are unable to agree as to the calculation or as to the adjustment to be made between the costs in favour of Blackbird and the sum payable to the liquidators, they may submit memoranda for my consideration. The matter should not be anything more than a straightforward calculation under the scale.

[63] Therefore my orders are:

(a) Blackbird shall pay the liquidators $6,876.15; and

(b) the liquidators shall pay Blackbird costs on the proceeding on a 2B basis.

Associate Judge R M Bell