IN THE HIGH COURT OF NEW ZEALAND
BLENHEIM REGISTRY

CIV 2007-406-004

	BETWEEN	DAVID SLIGO TAYLOR Plaintiff
	AND	SEAHORSE WORLD AQUARIUM Defendant

Hearing: 18-19 September 2007

Appearances: P J Radich with M Radich for Plaintiff
M Smith for Defendant

Judgment: 10 October 2007

JUDGMENT OF MACKENZIE J

Solicitors:
Radich Law, Blenheim for plaintiff
Michael Smith, Wellington for defendant

Introduction

[1] This is an application by the plaintiff for orders under s 174 of the Companies Act 1993 (the Act). That section provides:

> **174 Prejudiced shareholders**
>
> (1) A shareholder or former shareholder of a company, or any other entitled person, who considers that the affairs of a company have been, or are being, or are likely to be, conducted in a manner that is, or any act or acts of the company have been, or are, or are likely to be, oppressive, unfairly discriminatory, or unfairly prejudicial to him or her in that capacity or in any other capacity, may apply to the Court for an order under this section.
>
> (2) If, on an application under this section, the Court considers that it is just and equitable to do so, it may make such order as it thinks fit including, without limiting the generality of this subsection, an order—
>
> (a) Requiring the company or any other person to acquire the shareholder's shares; or
>
> (b) Requiring the company or any other person to pay compensation to a person; or
>
> (c) Regulating the future conduct of the company's affairs; or
>
> (d) Altering or adding to the company's constitution; or
>
> (e) Appointing a receiver of the company; or
>
> (f) Directing the rectification of the records of the company; or
>
> (g) Putting the company into liquidation; or
>
> (h) Setting aside action taken by the company or the board in breach of this Act or the constitution of the company.
>
> (3) No order may be made against the company or any other person under subsection (2) of this section unless the company or that person is a party to the proceedings in which the application is made.

[2] The orders sought are:

> 6.
>
> (i) For orders under Section 174 of the Companies Act:
>
> (a) Invalidating the purported forfeiture of their shares and restoring their shareholdings in the Defendant Company as at 1 July 2006.

(b) Invalidating the transaction between the Defendant Company and NZIJ Stockbrokers Limited.

(c) Invalidating the issue of shares which took place in August 2006 and restoring the shareholdings in the Company to those persons and in the numbers they were as at 1 July 2006.

(d) Removing the Second Defendant and the Third Defendant as Directors of the Company and replacing them with persons to be identified as being appropriate replacement directors and willing to so act.

(e) Any such other orders as the Court may deem to be appropriate under Section 174 of the Companies Act in order to ensure that the future affairs of the Defendant Company are undertaken in a manner consistent with the provisions of the Companies Act (including an order that the Defendant Company purchase the Plaintiffs' shares at their fair value before the conduct complained of took place or as if it had not taken place).

(f) Any such other orders as the Court may deem to be appropriate under Section 174 of the Companies Act in order to ensure that the depredations of the Second and Third Defendants on the Company and the Plaintiffs are remediated.

Background

[3] Sligo Enterprises Limited (the company) was formed in April 1989. Its name was changed in 2006 to Seahorse World Aquarium Limited. The capital of the company was 5,000 ordinary $1 shares, owned by Mr and Mrs Taylor. It was formed as a vehicle for business ventures by the Taylors. In 2001 it leased a site on the foreshore at Picton on which it established a public aquarium. The aquarium opened for business in March 2002. Mr and Mrs Taylor were both involved in its operation and their daughter was appointed manager.

[4] Concerns over Mrs Taylor's health prompted a decision in 2003 to reduce their involvement and the company was listed for sale. The estate agent introduced Mr Reuhman as a potential purchaser of a partial interest in the company. The proposal involved Mr and Mrs Taylor retaining an interest, with Mr Reuhman and some associates acquiring a partial interest and becoming involved in management. Negotiations were conducted over several months and culminated in three

agreements for sale and purchase of shares being entered into in September 2003. The agreements were all in similar form, and appear to have been prepared without the benefit of legal advice on either side. Under the three agreements, a total of 2,247 shares were sold by Mr and Mrs Taylor, for a price of $91 per share. The shares were acquired as follows:

a) NZIJ Stockbrokers Limited, a company associated with Mr Reuhman, as to 989 shares;

b) Seven Seas Consulting Limited, a company associated with Dr Mladenov, as to 159 shares; and

c) Marra Kaimoana Limited, a company associated with Mr David Tung, as to 1,099 shares.

[5] The remaining shares, 2,753, being 55% of the total, were retained by Mr Taylor as to 1,376 shares and Mrs Taylor as to 1,377. Subsequently, it appears that Mr and Mrs Taylor each sold 300 shares to Mr and Mrs Jackson. They have not featured in this litigation.

[6] Following purchase of the shares, Mr Reuhman, Dr Mladenov and Mr Tung were appointed directors, along with Mr and Mrs Taylor who each continued in that office. Dr Mladenov was appointed chairman. Mr Reuhman described himself as having effectively acted as an executive director from soon after the purchase, and said that he was formally appointed managing director from 1 February 2004 and has held that position since. Mr Taylor's evidence has a different perspective. He said that over the summer of 2003/04 Mr Reuhman took over day to day control of the aquarium while their daughter continued as manager. He said that he became concerned over difficulties which staff were experiencing with Mr Reuhman's management style, and with consultants' fees and expense claims made by Mr Reuhman. He raised those concerns in a letter to Dr Mladenov in late 2003. Dr Mladenov's evidence was that he received Mr Taylor's letter on 14 December 2003 and had several long telephone discussions with Mr Taylor listening to his concerns. It is clear that Dr Mladenov did not share Mr Taylor's views about Mr Reuhman.

[7] Mr Taylor said that a heads of agreement between the company and Mr Reuhman seeking to formalise Mr Reuhman's role within the company and to authorise salary payments of $40,000 per annum to Mr Reuhman, plus a performance incentive of 20% of the company's earnings before interest, tax, depreciation and amortisation. That agreement was to be for a term of three months unless superseded by a new agreement. Mr Taylor said that he had major objections to the agreement and communicated his concerns to Dr Mladenov. He said that a board meeting was held on 15 March 2004 to discuss the heads of agreement, that he expressed further concerns and that neither he nor his wife approved the agreement either as shareholders or directors, but that on 23 March 2004 he was informed by Dr Mladenov that he had signed and implemented the heads of agreement on behalf of the board. The minutes of the board meeting on 15 March 2004 record:

> Agreement with JPR – the board accepted the interim agreement with JPR to the end of April, although David Taylor noted that he disagreed with the incentive clause and wanted his negative vote registered in the minutes.

[8] In November 2003 Mr and Mrs Taylor had advanced $100,000 to the company secured by a debenture at an interest rate of 7% per annum for a period of two years. To repay that loan when it fell due in November 2005, a term loan was arranged between the company and NZIJ Stockbrokers Limited for the sum of $180,000, repayable on 31 March 2007 at an interest rate of 15.5% per annum. I deal in detail later with the circumstances of that transaction.

[9] In July 2006 Mr Reuhman called a meeting of the directors and shareholders by teleconference. A notice of intended shareholders and directors meeting scheduled for 25 July was sent by e-mail by Mr Reuhman on 10 July 2006. That was followed by a subsequent e-mail dated 15 July, altering the date to 27 July. Among the items referred to in the notices were shareholders resolutions, which Mr Taylor said were in the following form:

> *The 5,000 shares currently on issue in Sligo Enterprises are not fully paid.*
>
> *Resolution 1*
>
> *Resolved by the Shareholders and Directors of Sligo Enterprises Limited that the 5,000 shares currently be fully paid up by the shareholders at $1 per share by 5 pm on 31 July 2006.*

(Note the accountant has noted that the 5,000 shares in Sligo Enterprises have never been paid up and should be to tidy up affairs)

Sligo Enterprises' [sic] financial situation and future funding and resolution

Resolution 2

Resolved by the Shareholders and Directors of Sligo Enterprises Limited that the company issue 50,000 ordinary shares at $1 a share to the existing shareholders on a pro rata renounceable basis. Such shares to be fully subscribed for by 5 pm on 31 July 2006.

[10] I deal in more detail later with what occurred at that meeting. The minutes of the meeting record the relevant discussion in the following terms:

Paid up Capital
It was noted that all shareholders other than the Taylors had paid up their current shares. As previously indicated Dave Taylor advised that he and Lyn were seeking to have their shares paid up from monies owing to them. John advised that shareholders who had not paid up their existing shares would not be entitled to vote. It was recorded that a demand to pay would be made upon Dave and Lyn.

RESOLVED THAT:

1. Full payment of Shares
Resolved by the Shareholders and Directors of Sligo Enterprises Limited that the 5,000 shares currently issued be fully paid up by the shareholders at $1 a share by 5pm on 31 July 2006.

Moved by Phil Mladenov, seconded John Reuhman. Carried.

This was a unanimous resolution, noting the ineligibility of Dave and Lyn Taylor to vote.

2. Issue of Shares
Resolved by the Shareholders and Directors of Sligo Enterprises Limited that the company issue 50,000 fully paid ordinary shares at $1 a share to the existing shareholders on a pro rata renounceable basis. Such shares to be fully subscribed for by 5pm on 31 July 2006.

Moved by Phil Mladenov, seconded John Reuhman. Carried.

Shares in the new issue not taken up by existing shareholders are able to be taken up by shareholders who have fully subscribed to their entitlement. John Reuhman advised that the Jacksons and NZIJ Stockbrokers Ltd would take up further shares, and that there could be a premium payable by third parties taking up shares. Dave Taylor indicated that he and Lyn would not be taking up their entitlement in the new issue.

[11] Following that meeting, a demand of payment of $1,076 from Mr Taylor and $1,077 from Mrs Taylor was made. That notice required payment by 4:00 p.m. on 21 August 2006. No payment was made.

[12] Mr and Mrs Taylor gave written notice of their resignations as directors. The minutes of a meeting of directors held on 30 August 2006 record that the resignations received on 25 August effective that day were confirmed by unanimous resolution. The directors further resolved:

> Resolved by the directors of Sligo Enterprises Limited that pursuant to clause 13.3(1) of the company's constitution that the shares held by David Sligo Taylor and the shares held by Darryln Ann Taylor be and are forfeited.

[13] Those forfeited shares, recorded as 1,076 and 1,077 respectively, were transferred to the other shareholders pro rata.

The plaintiff's claims

[14] It is convenient to consider the claims by the plaintiff under three broad headings:

a) the forfeiture of the plaintiffs' shares;

b) the issue of new shares; and

c) the loan agreement with NZIJ Stockbrokers Ltd.

(a) The forfeiture of the plaintiffs' shares

[15] The plaintiffs submit that the actions of the directors in forfeiting the plaintiffs' shares for non-payment of call, effected by the resolution of 30 August 2006, is oppressive, discriminatory and unfairly prejudicial. A consideration of the plaintiffs' claims in this regard involves a consideration essentially of two issues:

a) whether a valid call was made on the shares.

b) whether (if the call was validly made) the shares were validly forfeited for non-payment of that call.

(a) Was the call validly made?

[16] That in turn involves two questions:

(i) was the capital unpaid;

(ii) was the resolution making the call properly passed.

(i) was the capital unpaid?

[17] The company was, as I have noted, incorporated in 1989. That was under the Companies Act 1955, under which shares were required to have a par value. The share capital of the company was 5,000 shares, each of $1. There is no evidence which is of assistance in determining whether the shares at that stage were issued as either:

a) fully paid shares, and if so how the consideration was paid, or

b) unpaid shares, and if so whether or not any call was made subsequent to the issue of those shares.

[18] The company must have been re-registered, or deemed to be re-registered, under the Companies Reregistration Act 1993. There is no evidence before the Court to establish whether that reregistration was effected by an application made under s 3 of that Act, or by a deemed reregistration under s 13 of that Act. It is thus not possible to ascertain, from the evidence before me, whether there was any uncalled or unpaid liability at the time of re-registration.

[19] The defendants' contention that the liability was unpaid rests on the way in which the share capital is shown in the annual accounts for the company. There were produced in evidence the annual accounts for the year ended 31 March 2005.

Those accounts were prepared by Winstanley Kerridge. Those accounts show the share capital and reserves as at 31 March 2005, and the comparative figures at 31 March 2004, as being zero, and for both years retained earnings being negative. Included in the current liabilities of the accounts, in both that year and the comparative for the previous year, are shareholders' current accounts totalling over $600,000. The accounts for the previous financial years were not produced in evidence. Dr Mladenov said in evidence, in answer to questions by me, that he had seen annual accounts before the agreement to purchase the shares was signed in 2003, but said that he could not remember whether those were for the year ended 31 March 2003 or whether the figures as to shareholders' funds and shareholders' current accounts were similar to those in the 2005 (and 2004 comparative) accounts.

[20] There are some indications in the evidence that the shares were fully paid, or at least were regarded by the parties as fully paid. In the first place, the agreements for sale and purchase of shares described the company as having an issued capital of $5,000 divided into "5,000 fully paid ordinary shares issued at $1 each". Furthermore, the agreements for sale and purchase are inconsistent with the capital structure of the company in the company's accounts. Under the agreements, the only assets to be acquired by the purchasers were the shares. The purchase price was $91 per share. That assumes that the company had substantial shareholders' funds. Those shareholders' funds might not be fully reflected in the company's accounts, because the value of the company's assets, including the value to be attributed to the business, might not be fully reflected in financial statements prepared on an historical cost basis of accounting. But while the figures in the accounts might well differ considerably from the sum agreed as purchase price, it is to be expected that for a purchase of shares at $91 per share, the broad capital structure would be that the bulk of the shareholder's interest in the company would be reflected in shareholders' funds rather than in current account loans due to them. That is not the situation as it appeared in the 2004 and 2005 accounts. It seems likely that that was not the structure in the 2003 accounts either.

[21] The vendors and the purchasers, apparently separately and without agreement between them as to the means of ensuring that the purchasers obtained the appropriate value for the shares being acquired, each adopted their own method for

achieving that result. Neither of those methods, for the reasons that I now describe, was legally effective to achieve the objective.

[22] Mr and Mrs Taylor, at about the time when the share sale agreements were signed, and while they remained the sole shareholders, purported to pass the following resolution:

> THAT a call of $1.00 per share having already been made, that call amounting to $5,000, a further call of $125.87 per share be, and hereby is, made on the holders of the 5,000 shares in the company. This further call will be payable by converting shareholder loans of $629,350 to share capital making the total share capital of the company $634,350.

[23] Two copies of that resolution were produced in evidence, each bearing a different date. I find on the evidence that a resolution in that form was passed by the shareholders, clearly with the objective of converting the shareholder loans to share capital. The effect of converting the shareholder current accounts to share capital would have been to align the capital structure with that appropriate to the agreement for sale and purchase, namely that the interest of Mr and Mrs Taylor in the company was all reflected in the value of their shareholding. It was, however, not legally possible to convert the shareholder current accounts to share capital in this way. Under the Companies Act 1955, the shares had been issued with a par value of $1. The liability of the holders of these shares was fixed by that, and it is only any unpaid part of that liability which would have carried on after reregistration. Under the 1993 Act, the consideration for which a share is issued must be specified when the shares are issued. It is simply not possible to make a further call on existing shares in the way in which this resolution purported to do.

[24] The purchasers adopted a different approach to the issue. Mr Reuhman, in a letter dated 29 August 2003 to Mr and Mrs Taylor, said:

> The Taylors will ensure that the accounts of Sligo Enterprises Limited are adjusted so that all the shareholders hold an equal and unfettered interest in Sligo (i.e. the current accounts and any advances are tidied up) in line with their shareholding.

The purported action stated for that portion of the letter was that Winstanley Kerridge were to advise. Subsequently, the accounts of the company were altered to

the effect that the shareholders' current accounts of over $600,000 were apportioned amongst all of the shareholders, in the accounts for the year ended 31 March 2004.

[25] Mr Kerr, in cross-examination, said that his understanding was that one of the requirements for the acquisition of shares by the purchasers was that the shareholders' current accounts be transferred to share capital and that is what that resolution was endeavouring to do. He said that there was a subsequent request from Mr Reuhman to sort out the current account, in a letter dated 19 December 2003 from Mr Reuhman to Mr Kerr. In response to that, Mr Taylor put through a book entry transferring the Taylors' shareholders' current accounts to all shareholders proportionately. That book entry took no account of the resolution passed earlier by Mr and Mrs Taylor. Mr Taylor said that there was an error on his part in that the resolution was overlooked when the current accounts were adjusted to meet Mr Reuhman's request.

[26] It is quite clear that that method too was legally ineffective. The shareholder current accounts represented debts owing by the company to Mr and Mrs Taylor. The acquisition of part of those debts by the purchasers would have required an agreement between the Taylors and the purchasers to assign part of the debt. It is clear that that did not occur. Mr Kerr made the alterations in the accounts, but, when pressed by me in the course of submissions, Mr Smith was unable to identify any transaction between the parties which would have justified those entries in the accounts. This method of dealing with the issue was also legally defective.

[27] The foregoing discussion is not directly relevant to the issue currently under consideration, namely whether the shares were fully paid to the extent of $1. There is, however, one relevant point on that issue which can be gleaned from the documentation, namely that the resolution passed by Mr and Mrs Taylor demonstrates their understanding that the shares were fully paid to the extent of $1. As they were the original shareholders in the company, evidence tending to show that that understanding was wrong would be necessary to establish, on the balance of probabilities, that the share capital was unpaid. I do not consider that there is evidence to establish that the proposition asserted both in the agreement for sale and purchase, and in that (albeit ineffective) resolution, namely that the shares were fully

paid, was wrong. Mr Smith submits that there were representations made by the Taylors to the effect that the share capital was unpaid and that they are estopped from asserting that the share capital was paid. That submission must fail, both on the facts and on the law. I find that no representation that the share capital was unpaid was made. The only statements made by Mr and Mrs Taylor on this point were to the effect that the share capital was paid. Further, as a matter of law, no estoppel could arise. The call had to be made by the company. The state of payment of its share capital must be capable of ascertainment by the company. The company could not properly place reliance on a representation by a shareholder on that issue. If the share capital was in fact paid, a debt could not arise from a representation from the shareholder to the company that it was unpaid. The submission based on estoppel is untenable.

[28] The question of whether the shares are fully paid or not is simply in an unsatisfactory state on the evidence available. It seems surprising that there would not be evidence available from the company's own records, or from the Companies Office documentation on the application for reregistration if there was one, that would shed further light upon the question. I am not able to make a finding either way. In the circumstances, as it is the defendants who have asserted an entitlement to make a call alleged to arise because the capital was unpaid, the onus is on the defendants to establish, on the balance of probabilities, that the share capital was not fully paid. That onus is not met. Accordingly, I hold that the call made on 27 July 2006 was not legally able to be made.

(ii) was the resolution making the call validly passed?

[29] In case I am wrong in that conclusion, and there was unpaid capital which could properly be the subject of a call, then I turn to consider whether the call made on 27 July 2006 was validly made. The making of a call on shares is a matter which, in the absence of contrary provision in the constitution, is for the directors, under s 47 of the Act. Mr and Mrs Taylor were both directors of the company at the time. The minutes of the meeting, set out in paragraph [10] above, show that they were held to be ineligible to vote. The minutes indicate that that resulted from advice

from Mr Reuhman that "shareholders who had not paid up their existing shares would not be entitled to vote". That advice was clearly wrong. In the first place, the vote required was one for the directors, not for the shareholders. Second, there can be no suggestion that Mr and Mrs Taylor were at that stage in default of any obligation in respect of their shares which might for some reason disentitle them to vote. The call had not been made, so no liability to pay had arisen. Third, it cannot be suggested that the fact that the resolution would have given rise to a liability on their part might have constituted an interest on their part which might disentitle them to vote. The call was being made on all shares, and affected all shareholders equally. The other shareholders had apparently made payments prior to the call being made, but that cannot affect voting rights.

[30] For these reasons, I find that if, contrary to my earlier finding, there was unpaid capital on the shares which could have been the subject of a call, no valid call was made. It follows that forfeiture for non-payment of the call could not have been effected.

(b) Were the shares validly forfeited for non payment of the call?

[31] If I am wrong in that conclusion, and the call was validly made, then the further question is whether the default in payment of that call constituted a basis upon which the shares might have been forfeited as was purported to be done by the resolution of 30 August. A right of forfeiture would have arisen only if that right was contained in the company's constitution. Such has been the lack of attention to the necessary and important legal requirements relating to this company that the parties are at issue even on the basic question of whether the company had a constitution at the relevant time.

[32] The adoption of a constitution is governed by s 32 of the Act. The shareholders may, by special resolution, adopt a constitution. The company had not, prior to December 2003, adopted a constitution. Dr Mladenov said in evidence that

> At no time did the Taylors question or query the existence of a company constitution despite reference being made to it on numerous occasions. To the contrary since I became associated with the company the Taylors have

> consistently represented that the company had a constitution. I never had reason to doubt these representations.

[33] Dr Mladenov was cross-examined about that proposition. It is unnecessary for me to examine the question in detail. I find that no such representation was made, and that Dr Mladenov could not properly have drawn such an inference from the matters on which he relied. But in any event, that is beside the point. A constitution cannot be adopted by representation. For that reason, the claim of estoppel raised by the defendants on this issue must also fail.

[34] The question of a constitution was raised at a board meeting on 11 December 2003 where the following is recorded:

> Constitution – constitution needs to be formally adopted, this has been mentioned at previous to board meetings, JR has already spoken to Steve Riley at Londons about the constitution (action – JR).

[35] The evidence was that the issue of a constitution had been raised by Mr Taylor, who had produced the Avon form of constitution and suggested that consideration be given to adopting it. The matter was again raised at a directors meeting on 15 January 2004 where the following note appears in the minutes:

> Company constitution – adopted Avon constitution as presented by JR.

[36] Clearly, those were matters which involved the directors only. The directors did not have the legal power to adopt the constitution. The defendants submit that all the directors were also shareholders, and that the actions can be taken to be actions of the shareholders as well as of the directors. The actions which were taken at those two meetings cannot amount to the adoption of a constitution by special resolution of the shareholders. Some degree of informality in the way in which company procedures are carried out may be able to be countenanced. To treat those resolutions as amounting to sufficient compliance with the procedures for proposing and passing a special resolution would go far beyond the bounds of what could properly be regarded as substantial compliance. It is also of note that s 32 requires notice of the adoption of a constitution to be registered. That was not done at that time. A constitution was subsequently adopted, but not until October 2006. The

notice of adoption registered at that time records that action as the adoption of a constitution, not an alteration or revocation of a previous constitution.

[37] Mr Smith argues in the alternative, that if the constitution was not validly adopted in December 2003, then the actions of the parties were sufficient to give rise to a contract between the shareholders and the company, giving rise to a right of forfeiture of shares. Mr Smith refers to *Shalfoon v Cheddar Valley Co-operative Dairy Co Ltd* [1924] NZLR 561. He relies upon the following statement by Salmond J in that decision:

> There are two distinct ways in which an obligation may come into existence as between a company and one of its shareholders. In the first place, it may have its source in a regulation validly made by the company and inserted in the Articles of Association in pursuance of the authority conferred by ss 22 and 122 of the Companies Act 1908. In the second place it may have its source in a contract made between the company and the individual shareholder.

[38] That general proposition remains valid under the present legislation, where the function of the Articles of Association may be performed by a constitution. But there is no evidence here to establish the existence of a contract between Mr and Mrs Taylor and the company to the effect that their shares could be forfeited for non-payment of calls. It would be necessary to show that there was a contract not just between the company and Mr and Mrs Taylor, but also between the company and all other shareholders, since it would be quite unrealistic to attribute to Mr and Mrs Taylor an intention to agree that their shares could be forfeited, when the shares of others could not, in similar circumstances, be forfeited. The evidence simply does not establish anything of the sort, nor could a right of forfeiture arise from estoppel, as Mr Smith submitted. The proposition that there is a contractual right to forfeit the shares, independent of a constitution, is simply untenable.

[39] For these reasons, I am satisfied that no right to forfeit shares existed, even if, contrary to my earlier findings, Mr and Mrs Taylor were in default of an obligation to pay a call on those shares.

(b) The issue of new shares

[40] The second resolution purportedly passed at the telephone meeting of 27 July 2006 was a resolution to issue new capital. Mr Taylor's evidence is that the notice of meeting stated that all the other shareholders, apart from himself and his wife, had agreed to take up their entitlements under the proposed issue. The document setting out the resolutions and that further statement is not in evidence before me. I accept Mr Taylor's evidence as to the form of the resolutions (set out in paragraph [9] above), as it is unchallenged on this point. Mr Taylor says that he and his wife refused to vote for either of the resolutions. He says that they were in an invidious position in relation to the issue of further shares in that they firmly opposed it as they knew that any capital raised was going directly to NZIJ but that if they refused to subscribe their position as major shareholders would be diluted and their shareholding would become worthless. His evidence was that all of this was sprung on them at short notice.

[41] Mr Taylor was cross-examined as to the claim that a reasonable time was not given to take up the new shares, in that the two working days available to take up the shares following passing of the resolution was not a reasonable time. It was put to him in cross-examination that he had consistently from early 2004 made known to the company that the Taylors would not invest any further money in the company either by way of equity or debt, and he accepted that proposition. It was then put to him that if he had taken that stand and was resolute in the position that he would not purchase the shares there could be no unfair prejudice. In dealing with the evidence, it is sufficient to note, from that exchange in cross-examination, that I find that Mr Taylor had made the Taylors' unwillingness to invest further capital in the venture known prior to the proposing of those resolutions. It is unnecessary for me to decide whether the actions of the defendants in proposing the increase in capital in the face of that known unwillingness were oppressive or unfairly prejudicial in terms of s 174, because (as I have held at paragraph [29]), Mr and Mrs Taylor were wrongly held to be ineligible to vote at the meeting of 27 July 2006, and it necessarily follows from that finding that the resolution purporting to issue new shares was not properly passed.

(c) The loan agreement with NZIJ Stockbrokers

[42] As I have described in paragraph [8], a loan was arranged in November 2005 from NZIJ Stockbrokers Ltd, partly to replace an advance from the Taylors. Instructions to prepare the documentation were given by Mr Reuhman, in his capacity as a director of NZIJ, to that company's solicitor by letter dated 28 October 2005. The letter is revealing as to the state to which relations between the parties had deteriorated, and as to Mr Reuhman's opinion of Mr Taylor at that stage. The letter said:

> The Taylors can be very difficult. Dave Taylor is a classic passive aggressive and is slowly going nuts and deaf. In April he served fellow director, Dr Phillip Mladenov for allegedly not honouring an agreement to pay $4,000. He also sued Sligo for about $20,000 for alleged interest arrears. It was all settled and no payments were required as Taylor had previously agreed to the events that caused him to take action. The air was blue at the May board meeting and Taylor just smiled like an idiot. Taylor agreed at the May meeting to extend the $100,000 loan until 31 March 2006. Then out of the blue changed his mind in September.

[43] The terms of the loan were also set out in a document, the provenance of which is unclear, dated 25 October 2005 in which it is recorded that the purpose of the loan was as to $100,000 to replace the Taylor finance, as to $40,000 to replace an NZIJ loan, and as to $40,000 to repay an NZIJ outstanding account. Mr Taylor's evidence is that neither he nor Mrs Taylor were aware of the NZIJ transaction or asked to approve it, nor were they informed of its terms and in particular were not aware of the 15.5% interest rate. His evidence is that they did not approve the transaction in their capacity as either shareholders or directors; that they were unaware that it had been entered into by the company; that neither he nor his wife had seen that loan agreement until Mr Reuhman provided a copy to their solicitors in late 2006; and that their understanding was that the funding had been provided by Westpac. He said that the first time they saw the document dated 25 October 2005 was also in late 2006.

[44] There is no evidence that the terms of the loan or the identity of the lender were approved by the directors or the shareholders before the loan was entered into. Mr Reuhman's evidence was that the terms and conditions of the loan were discussed in detail at the board meeting of 17 December 2005. But the loan

agreement had already been entered into by then. The funds had been advanced, and the Taylor loan had been repaid. Dr Mladenov in his evidence said that at a board meeting on 15 May 2005 the Taylors had agreed to postpone repayment of their loan from 1 November 2005 to 1 April 2006, but that by letter dated 21 August 2005 resiled from that agreement. He says that he accepted that and the company got on with arranging a loan to repay the Taylors on 1 November 2005. He did not say that the terms of the loan which was arranged were ever discussed or approved by the board prior to its being entered into.

[45] Mr Taylor's evidence was that he understood that the replacement finance was being arranged from Westpac. The defendants challenge that, by pointing to evidence that the material from Westpac concerning the possibility of a loan indicated that shareholder guarantees would be necessary, and that Mr and Mrs Taylor were unwilling to give those guarantees, and never disclosed their financial position as would have been required. It is not necessary for me to reach any conclusion as to whether any assumption as to the identity of the lender was made by the Taylors, or whether any assumption which they made was reasonable or not. The essential issue is whether, as directors and shareholders, they were aware of the identity of the lender, which was in fact a shareholder of the company, and a company in which Mr Reuhman, a director, had an interest. I find that the evidence establishes quite clearly that they were not informed of that prior to the transaction being entered into. A further aspect of the transaction was that $80,000 of the funds which were borrowed were used to pay debts apparently owing to the lender. Mr and Mrs Taylor were not made aware of that aspect of the transaction before it was entered into.

[46] Mr Radich submits that this transaction was entered into by Mr Reuhman and Dr Mladenov as signatories of the company and that the transaction was not effected pursuant to a resolution of directors or following disclosure in terms of the related party provisions of the Act. I find that to be so. The evidence establishes that Mr Reuhman has a material financial interest in NZIJ. He was accordingly "interested" in the transaction between the company and NZIJ, in accordance with s 139 of the Act. Section 140 accordingly required a disclosure of his interest in that transaction to the board of the company. I find that no such disclosure was made.

Mr Reuhman's interest in NZIJ was known to all directors, but the transaction was not. The transaction between the company and NZIJ was not disclosed to the board of the company before it was entered into. The provisions of s140 were not complied with.

[47] It is necessary to consider the implications of that finding in relation to the plaintiff's application under s 174. Mr Smith submits that no prejudice to the plaintiff as a result of this transaction is established. He submits that the only prejudice identified by Mr Taylor in evidence was the detriment suffered by the company as a consequence of having to pay a high interest rate on the borrowings from NZIJ. I consider that circumstances to which I have referred in paragraphs [44] and [46] are such that the failure to disclose this transaction does fall within the classification of an act of the company which has been unfairly discriminatory of the plaintiff in terms of s 174, by reason of the circumstances in which that loan was taken out. While the transaction was one between NZIJ and the company, and was not one which directly affected the shareholders, the fact that the lender was a shareholder, and that the funds were borrowed from a shareholder in the company, replacing a loan from another shareholder, at a considerably higher interest rate, do cause this transaction to fall into the category of transactions to which s 174 applies.

Decision as to the application of s174

[48] For these reasons, I find that, on all three grounds relied on by the plaintiff, the circumstances for granting relief under s174 are made out.

Relief

[49] The present situation which has been reached in the affairs of the company is, as Mr Radich aptly described it, "a mess". Even without recourse to s 174, the transactions by which the shareholders' current accounts were transferred have been shown to be ineffective, the call on the plaintiff's shares was not validly made, the forfeiture of the plaintiff's shares has been improperly effected, the new capital has not been validly issued, and there has been a breach of the related party provisions. The question is, what should now be done to remedy the situation. The range of

orders which the Court is able to make is set out in s 174(2). Mr Radich submitted that it may be appropriate, if I were to conclude that relief under s 174 is available, to defer the granting of relief for further consideration, to give the parties an opportunity to assess the position in the light of this judgment. I consider that that is the appropriate course to be followed.

[50] In the first place, for the reasons I have given, I consider that the cancellation of the plaintiff's shares, and the issue of the new capital, are invalid, in that they were not properly effected. The interest in the company which the plaintiffs held prior to those transactions must be restored. I do not consider that recourse to s 174 is necessary to achieve that result, but relief may be a convenient mechanism for that purpose. Any relief which is granted under s 174 will need to take account of the invalidity of the procedures by which the plaintiffs were deprived of their interest in the company. Any relief granted under s 174 must recognise their interest, and the relief must include such measures as may be appropriate to restore the situation.

[51] It appears quite clear that relations between the parties have irretrievably broken down. It will be for the parties to assess how best to move forward. The parties will need to assess whether they can co-operate in the future as ongoing joint shareholders, or whether some solution which would involve the acquisition, at fair value, of the interests of one or more of the shareholding groups by the others would be a more realistic outcome. The relief which is appropriate under s 174 may differ depending upon whether or not agreement can be reached as to a broad forward strategy, and if so, upon which of the available options that strategy may adopt.

[52] In leaving the matter for further consideration by the parties, as I propose to do, I must urge upon the defendants the need to adopt a realistic approach, and one which recognises the legitimate interests of the plaintiffs as shareholders in this company. That is desirable because a solution which is determined by the parties is more likely to achieve a satisfactory outcome for all concerned than if Court were to invoke some of the more extreme forms of relief for which s 174 provides. I consider that the evidence, and the litigation itself, shows a disregard for the legitimate concerns and the rights of the plaintiffs. I have felt it appropriate to speak

bluntly, because of my concern that, unless a more conciliatory and realistic approach is adopted, recourse to those more extreme powers may be unavoidable.

Result

[53] For the reasons I have given, I make a declaration that the affairs of the company have been conducted in a manner that is oppressive, unfairly discriminatory or unfairly prejudicial to the plaintiff in its capacity as shareholders, and that it is just and equitable that relief be granted under s 174(2). I adjourn for further consideration the issue of what relief is appropriate. The proceedings may be brought on before me by any party on 14 days notice.

[54] Costs are reserved.

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A.D. MacKenzie J